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In The
# Supreme Court of the United States

KATHI COOPER, et al.,

*Petitioners,*

v.

IBM PERSONAL PENSION PLAN & IBM CORP.,

*Respondents.*

**On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit**

## PETITION FOR A WRIT OF CERTIORARI

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## QUESTIONS PRESENTED

Section 204(b)(1)(H)(i), 29 U.S.C. § 1054(b)(1)(H)(i), of the Employee Retirement Income Security Act ("ERISA"), provides that a defined-benefit pension plan violates the Act's proscription against age discrimination if "the rate of an employee's benefit accrual is reduced, because of the attainment of any age."

Respondents' defined benefit pension plan uses a "cash balance formula" to calculate benefits, under which an employee's pension entitlement attributable to any single year of work decreases depending upon how close in age the employee is to the normal retirement age of 65. The formula accomplishes this result by adding a hypothetical "interest credit" to each employee's fictional account for each year of the employee's age below retirement age, thus giving younger employees more interest credits and greater pension entitlements than older employees. Respondents' pension plan also credited younger employees an unearned increase to their opening cash balance accounts but limited older employees to their vested benefits under the prior plan.

The questions presented are:

Whether a defined benefit plan using a cash balance formula violates ERISA Section 204(b)(1)(H)(i) because an employee's rate of benefit accrual decreases the closer he is to retirement age.

Whether a defined benefit plan that gave younger employees an unearned increase in their opening cash balance accounts that was denied to older employees violated ERISA Section 204(b)(1)(H)(i).

## PARTIES TO THE PROCEEDING

The petitioners in this Court include Kathi Cooper and Beth Harrington as class representatives of the class of IBM pension plan participants certified by the district court. The class has more than 250,000 current and retired IBM employees. They were plaintiffs in the district court and appellees before the court of appeals.

The respondents in this Court are IBM Corporation and IBM Personal Pension Plan. They were the defendants in the district court and the appellants before the court of appeals.

## TABLE OF CONTENTS


| | Page |
|---|---|
| QUESTIONS PRESENTED | i |
| PARTIES TO THE PROCEEDING | ii |
| TABLE OF CONTENTS | iii |
| TABLE OF AUTHORITIES | v |
| PETITION FOR A WRIT OF CERTIORARI | 1 |
| OPINIONS BELOW | 3 |
| JURISDICTION | 3 |
| STATUTORY PROVISIONS INVOLVED | 3 |
| STATEMENT OF THE CASE | 4 |
| REASONS FOR GRANTING THE WRIT | 13 |
| I. REVIEW IS WARRANTED OF THE SEVENTH CIRCUIT'S ERRONEOUS CONCLUSION THAT RESPONDENTS' DEFINED BENEFIT PENSION PLAN DOES NOT VIOLATE ERISA'S PROHIBITION AGAINST AGE DISCRIMINATION | 14 |
| A. The Seventh Circuit Ignored the Plain Meaning of ERISA's Test for Impermissible Age Discrimination | 15 |
| 1. A Defined Benefit Plan Using a Cash Balance Formula Is Not Economically Equivalent to a Defined Contribution Plan | 16 |
| 2. Judge Easterbrook's Opinion Misconstrued the Term "Employee's Rate of Benefit Accrual" To Mean "Employer's Rate of Contribution" | 18 |

TABLE OF CONTENTS – Continued

Page

B. The Seventh Circuit's Decision Conflicts with Decisions of the Second, Ninth, and Eleventh Circuits ..... 22

C. The Legal Issues Presented by this Case Are Important ..... 27

II. THE SIXTH AND SEVENTH CIRCUITS CONFLICT ON THE LEGALITY OF BENEFIT INCREASES PROVIDED ONLY TO YOUNGER EMPLOYEES ..... 28

CONCLUSION ..... 30

APPENDIX

Court of Appeals Opinion ..... App. 1

District Court Opinion ..... App. 14

District Court Final Judgment ..... App. 42

Court of Appeals Order Denying Rehearing and Rehearing *En Banc* ..... App. 45

## TABLE OF AUTHORITIES

Page

CASES

*Berger v. Xerox Corp. Retirement Income Guaranty Plan*, 338 F.3d 755 (7th Cir. 2003) ..... 4, 5, 7

*Cooper v. IBM Personal Pension Plan*, 274 F. Supp.2d 1010 (S.D. Ill. 2003) ..... 3

*Cooper v. IBM Personal Pension Plan*, 457 F.3d 636 (7th Cir. 2006) ..... 3

*Drutis v. Quebecor World (USA), Inc.*, 2006 U.S. Dist. LEXIS 84950 (E.D. Ky. Sept. 25, 2006), *appeal pending*, No. 06-6380 (6th Cir.) ..... 26

*EEOC v. Jefferson County Sheriff's Dept.*, 467 F.3d 571 (6th Cir. 2006) (*en banc*) ..... 29

*Esden v. Bank of Boston*, 229 F.3d 154 (2d Cir. 2000) ..... *passim*

*Hirt v. Equitable Retirement Plan*, 441 F. Supp. 2d 516 (S.D.N.Y. 2006) ..... 26

*Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432 (1999) ..... 5, 16

*J.P. Morgan Chase Cash Balance Litigation, In re*, 2006 WL 3063424 (S.D.N.Y. Oct. 30, 2006) ..... 20, 25

*Laurent v. PriceWaterhouseCoopers LLP*, 448 F. Supp. 2d 537, 2006 WL 2546805 (S.D.N.Y. Sept. 5, 2006) ..... 25

*Lyons v. Georgia-Pacific Corp. Salaried Employees Ret. Plan*, 221 F.3d 1235 (11th Cir. 2000), *cert. denied*, 532 U.S. 967 (2001) ..... 22, 23, 24

*Miller v. Xerox Corp. Retirement Income Guarantee Plan*, 464 F.3d 871 (9th Cir. 2006) ..... 22, 24

TABLE OF AUTHORITIES – Continued

Page

*Register v. PNC Fin. Servs. Group, Inc.*, 2005 WL 3120268 (E.D. Pa. Nov. 21, 2005), *appeal pending*, 3d Cir. No. 05-5445 ..... 26

*Richards v. FleetBoston Financial Corp.*, 427 F. Supp. 2d 150 (D. Conn. 2006) ..... 25

*Richards v. FleetBoston Financial Corp.*, 2006 WL 3000768 (D. Conn. Oct. 16, 2006) ..... 25

STATUTES

28 U.S.C. § 1254(1) ..... 3

29 U.S.C. § 1002(23) ..... 6, 16

29 U.S.C. § 1002(34) ..... 6

29 U.S.C. § 1054(b)(1)(H)(i) ..... *passim*

29 U.S.C. § 1054(b)(2) ..... 4, 16

29 U.S.C. § 1054(c)(3) ..... 5

Consolidated Appropriation Act of 2004, P.L. 108-109, § 205 ..... 21

Pension Protection Act of 2006, P.L. 109-280, § 701 .... 2, 27

MISCELLANEOUS

Pension Benefit Guaranty Corp., Pension Insurance Data Book for 2005, http://www.pbgc.gov/docs/2005databook.pdf ..... 2

Zelinsky, *The Cash Balance Controversy*, 19 Va. Tax Rev. 683 (2000) ..... 5

TABLE OF AUTHORITIES – Continued

Page

Zelinsky, *The Defined Contribution Paradigm*, 114 Yale L. J. 451 (2004) ..... 5

Zelinsky, *Cooper v. IBM Personal Pension Plan*, Social Science Research Network, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=926560 (2006) .... 4, 17, 18, 19

## PETITION FOR A WRIT OF CERTIORARI

The Seventh Circuit's decision below is enormously important because it threatens to deprive millions of older Americans of congressionally-enacted protections against age discrimination in their pension plans. The court of appeals upheld a pension benefit formula used by one of the nation's largest companies that admittedly provides lower pension benefits to older employees than younger employees with the same service and salary history, notwithstanding the express nondiscrimination mandate of the Employee Retirement Income Security Act ("ERISA") condemning that result.

No one disputes that under respondents' formula an older employee who does the same work as a younger employee for the same salary accrues pension benefits attributable to that year's work at a rate that is lower than the rate at which the younger employee accrues benefits. Nor is there any dispute that the exclusive reason for the different entitlement is the older employee's age, in particular that he is closer to normal retirement age. As demonstrated by the record in this case, respondent IBM understood precisely what the actuarial effect was of its policy, including its intended and discriminatory impact in terms of the age of its employees, which its formula then fully realized.

Also undisputed are the monetary significance of the resulting discrimination and the extent to which such discrimination is widespread in existing cash balance plans. The parties stipulated that if the courts agreed that the discrimination violated ERISA, petitioners were entitled to $1.4 billion in increased benefits from respondents. That striking amount, however, is literally just the tip of the iceberg of those adversely affected by the Seventh Circuit's decision. Nationwide there are more than

eight million employees of companies that have similar pension plans.[1]

The multiple flaws in the Seventh Circuit's reasoning also present important legal issues warranting this Court's immediate attention. In an opinion written by Judge Frank Easterbrook, the lower court ignored the plain meaning of the statutory language, replaced the legal definition supplied by Congress for unlawful age discrimination with the court's own economic theories about age discrimination, and erroneously equated two distinct kinds of pension plans (defined-*benefit* plans and defined-*contribution* plans) that are fundamentally different in their economic operation and, even more significant, in their treatment under ERISA. The court's rulings in these respects conflict with the decisions of other circuit courts arising under ERISA. Unlike Judge Easterbrook, those courts have recognized the distinctions that Congress carefully drew in ERISA between defined benefit plans and defined contribution plans, and those other courts have concluded that plans such as IBM's Plan that use a cash balance formula are governed by ERISA's requirements for defined benefit plans.

Finally, neither Congress's recent amendment of ERISA (*see* Pension Protection Act of 2006, P.L. 109-280, § 701) nor the existence of several other cases pending in the lower courts raising similar legal issues provides reason to delay this Court's review. The congressional amendment is prospective only and does not affect the rights of millions of employees, including petitioners here. The ongoing lower court litigation merely underscores the existing and increasing significance of the legal issues raised in this case, notwithstanding the recent congressional enactment. It would, moreover, be especially unjust

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[1] The Pension Benefit Guaranty Corp., Pension Insurance Data Book for 2005, http://www.pbgc.gov/docs/2005databook.pdf, at 61, 62.

for the Court to delay ruling on the legal issues presented, thereby forever precluding the 250,000 members of the class represented by petitioners in this case from recovering for what the Court later concludes is unlawful age discrimination. The current case presents the legal issue in a clear and unencumbered manner and no further lower court consideration is warranted prior to this Court's plenary review.

## OPINIONS BELOW

The opinion of the district court granting summary judgment in favor of petitioners on the issue of liability (App. 14-41) is reported at 274 F. Supp. 2d 1010. The opinion of the court of appeals (App. 1-13) is reported at 457 F.3d 636.

## JURISDICTION

The judgment of the court of appeals was entered on August 7, 2006. Petitions for rehearing and rehearing en banc were denied on September 1, 2006. App. 45. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

## STATUTORY PROVISIONS INVOLVED

This case concerns the meaning of two subsections of Section 204(b) of the Employment Retirement Security Act (ERISA), 29 U.S.C. § 1054(b).

Section 204(b)(1)(H)(i) governs age discrimination in defined benefit plans and provides in pertinent part:

> [A] defined benefit plan shall be treated as not satisfying the requirements of this paragraph if, under the plan, . . . the rate of an employee's benefit accrual is reduced, because of the attainment of any age.

ERISA Section 204(b)(2)(A) governs age discrimination in defined contribution plans and provides in pertinent part:

> A defined contribution plan satisfies the requirements of this paragraph if, under the plan, . . . the rate at which amounts are allocated to the employee's account is not reduced, because of the attainment of any age.

## STATEMENT OF THE CASE

1. ERISA permits employers to choose one of two fundamentally different plan designs to take advantage of the tax incentives provided for "qualified" pension plans. One option is to create *a defined contribution* plan (such as the widely used 401(k) plan), in which the employer typically contributes a percentage of the employee's compensation annually to an investment account created for the employee. The employee's pension entitlement is the value of his account, consisting of the employer's annual contributions plus any earnings flowing from the employee's investment of those deposits. *See Berger v. Xerox Corp. Retirement Income Guarantee Plan*, 338 F.3d 755, 758 (7th Cir. 2003). The employee owns the funds in the account and bears the investment risk. Because an employer's obligation under such a plan extends only to the annual contribution to the employee's account, ERISA's age discrimination rule for defined contribution plans requires only that an employer contribute an equal percentage of salary to each employee's account regardless of age. ERISA Section 204(b)(2)(A), 29 U.S.C. § 1054(b)(2)(A). *See generally* Zelinsky, *Cooper v. IBM Personal Pension Plan*, Social Science Research Network, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=926560, at 3-12 ("Zelinsky Cooper Critique").[2]

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[2] Professor Edward A. Zelinsky is a leading legal scholar with respect to pensions in general and the cash balance formula in particular.

(Continued on following page)

The employer's other option is to create *a defined benefit* plan in which the employer promises to pay an employee a guaranteed benefit amount at "normal retirement age." This benefit is typically calculated as a percentage of the employee's compensation (averaged over a specified time period or the employee's entire career) times his years of service. The pension entitlement provided by the plan is the "accrued benefit" at normal retirement age (which the plan selects but cannot be later than age 65). *Berger*, 338 F.3d at 758. ERISA requires that the accrued benefit be provided in the form of an annuity at normal retirement age. ERISA Section 204(c)(3), 29 U.S.C. § 1054(c)(3). A plan may offer optional benefit forms, such as a lump sum, but the benefits paid out cannot be less than the actuarial equivalent of the annuity at normal retirement age. *Berger*, 338 F.3d at 759; *see also Esden v. Bank of Boston*, 229 F.3d 154, 162-164 (2d Cir. 2000). The employee does not own any of the plan's assets but instead has a contract right to be paid benefits at normal retirement age as provided by the plan's terms. Consistent with the requirement that an employee's pension entitlement is the accrued benefit at normal retirement age, the age discrimination rule applicable to defined benefit plans prohibits any cessation or reduction in the rate at which an employee accrues this benefit on account of age. ERISA Section 204(b)(1)(H)(i), 29 U.S.C. § 1054(b)(1)(H)(i).

This Court, in *Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 439-440 & n.3 (1999) (citations omitted), explained these fundamental differences between defined contribution and defined benefit plans:

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*See* Zelinsky, *The Defined Contribution Paradigm*, 114 Yale L. J. 451 (2004); Zelinsky, *The Cash Balance Controversy*, 19 Va. Tax Rev. 683 (2000).

> A defined contribution plan is one where employees and employers may contribute to the plan, and "'the employer's contribution is fixed and the employee receives whatever level of benefits the amount contributed on his behalf will provide.'" . . . A defined contribution plan "provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant's account." ERISA § 3(34); 29 U.S.C. § 1002(34). . . .
>
> A defined benefit plan, on the other hand, consists of a general pool of assets rather than individual dedicated accounts. Such a plan, "as its name implies, is one where the employee, upon retirement, is entitled to a fixed periodic payment." . . . [T]he employer typically bears the entire investment risk and – short of the consequences of plan termination – must cover any underfunding as the result of a shortfall that may occur from the plan's investments. . . .
>
> . . . [Defined benefit plan] members have a right to a certain defined level of benefits, known as "accrued benefits." That term, for purposes of a defined benefit plan, is defined as "the individual's accrued benefit determined under the plan [and ordinarily is] expressed in the form of an annual benefit commencing at normal retirement age." ERISA § 3(23)(A), 29 U.S.C. § 1002(23)(A). . . .
>
> . . . .
>
> By contrast, an "accrued benefit" for purposes of defined contribution plans means "the balance of the individual's account." ERISA § 3(23)(B), 29 U.S.C. § 1002(23)(B).

In an effort to circumvent ERISA's sharp distinction between defined benefit and defined contribution plans, numerous employers have amended their defined benefit plans to adopt a "cash balance formula" (often referred to as a "cash balance plan"). The formula describes the employee's

benefit in a manner designed to resemble the operation of a defined contribution plan even though the plan legally remains a defined benefit plan. *Esden*, 229 F.3d at 158. The typical cash balance formula purports to compute an employee's "accrued benefit" as a hypothetical account balance, to which putative "pay credits" and "interest credits" are added each year. In reality, "the employee has no actual account, the employer makes no contributions to an employee account, and so there is no account balance to which interest might be added." *Berger*, 338 F.3d at 758. Rather, the employee's pension entitlement under a cash balance formula remains the accrued benefit earned each year, which equals the amount of both that year's pay credit and the value of the future "interest credits" on that amount through the employee's normal retirement age, divided by an annuity factor specified in the plan. *Id.* at 758-759; *Esden*, 229 F.3d at 158-159. In short, the cash balance formula differs from traditional defined benefit formulas only by injecting hypothetical steps into the calculation of the accrued benefit. In the end, it is simply a mathematical formula that calculates a retirement benefit.

The following chart shows the accrued benefit an employee earns each year under a cash balance formula providing a 5% pay credit and a 5% interest credit for differently aged employees earning $50,000 per year, using a typical annuity conversion factor of 10.

| Age | Pay Credit Projected to 65 | Annual Accrued Benefit at 65 | Accrued Benefit as % of Pay |
|---|---|---|---|
| 25 | 17,600 | 1,760 | 3.52% |
| 35 | 10,800 | 1,080 | 2.16% |
| 45 | 6,633 | 663 | 1.33% |
| 50 | 5,197 | 520 | 1.04% |
| 55 | 4,072 | 407 | 0.81% |
| 60 | 3,191 | 320 | 0.64% |
| 64 | 2,625 | 262 | 0.53% |

The result of this formula is that as an employee advances a year in age the rate of benefit accrual decreases both as a dollar amount and as a percentage of pay.

Under this formula, the actual amount of the accrued benefit – and the rate of accrual of that benefit – are always smaller for an older employee than for a younger employee with the same salary and service history. *See* IBM's 7th Cir. Appendix ("CA App.") at 380-381. This accrual pattern is identical to what would result from a conventional defined benefit plan that expressly provided that the accrued benefit equals a declining percentage of each year's pay for each year that an employee ages (*i.e.*, a 25-year-old employee accrues a benefit equal to 3.52% of pay, while a 45-year-old accrues a benefit equal to 1.33% of pay and a 64-year-old accrues a benefit equal to .53% of pay). IBM candidly admitted (IBM 7th Cir. Reply Br. 14) that a traditional defined benefit plan that provided such a declining rate of benefit accrual would violate ERISA Section 204(b)(1)(H)(i).

2. IBM's Plan adopted a cash balance formula effective July 1, 1999. CA App. 213. The formula determines a participant's benefit by reference to "pay credits" of 5% of each year's salary to a participant's hypothetical Personal Pension Account ("PPAcct") as well as annual "interest credits" on its dollar amount at the rate of the one-year Treasury bill rate plus 1% to the PPAcct. *Id.*, 242-243. The Plan states that the resulting account balance constitutes a participant's accrued benefit. *Id.*, 240, § 11.1. If a participant defers the receipt of benefits until normal retirement age, the participant is entitled to an annuity, which is the "default" benefit form, calculated by dividing the hypothetical PPAcct by an annuity factor provided in the Plan. *Id.*, 245, § 12.2(b).

IBM's actuaries undertook an "Age Discrimination Analysis" of the cash balance formula prior to its adoption. Plaintiffs-Appellees' 7th Cir. Supplemental Appendix ("CA Supp. App.") 76. Part of the Analysis focused on the age-65 annuities that would be earned by employees with the same salary and years of service but with different ages. The results showed that the increase in the age-65 annuity earned each year under the cash balance formula, *i.e.*, the rate of benefit accrual, for the younger employee exceeded the rate for the older employee. In addition, the amount of the annuity earned each year by an employee decreased as the employee aged. *Id.*, 79-86. The following chart illustrates these effects of IBM's cash balance formula. It shows the annual rate of benefit accrual for differently aged employees using a 5% pay credit and a 5.5% interest credit (the initial applicable rate under IBM's formula, CA App. 391).

| Age | Accrual Rate | Age | Accrual Rate | Age | Accrual Rate |
|---|---|---|---|---|---|
| 21 | 4.667% | 36 | 2.090% | 51 | 0.936% |
| 22 | 4.423% | 37 | 1.981% | 52 | 0.887% |
| 23 | 4.193% | 38 | 1.878% | 53 | 0.841% |
| 24 | 3.974% | 39 | 1.780% | 54 | 0.797% |
| 25 | 3.767% | 40 | 1.687% | 55 | 0.756% |
| 26 | 3.571% | 41 | 1.599% | 56 | 0.716% |
| 27 | 3.384% | 42 | 1.516% | 57 | 0.679% |
| 28 | 3.208% | 43 | 1.437% | 58 | 0.644% |
| 29 | 3.041% | 44 | 1.362% | 59 | 0.610% |
| 30 | 2.882% | 45 | 1.291% | 60 | 0.578% |
| 31 | 2.732% | 46 | 1.224% | 61 | 0.548% |
| 32 | 2.589% | 47 | 1.160% | 62 | 0.520% |
| 33 | 2.454% | 48 | 1.099% | 63 | 0.492% |
| 34 | 2.327% | 49 | 1.042% | 64 | 0.467% |
| 35 | 2.205% | 50 | 0.988% | 65 | 0.442% |

As the chart shows, the rate of benefit accrual for participants in IBM's plan declines steeply solely on the basis of their age. The oldest participant's benefit accrual rate is less than 10% of a 21-year-old participant's benefit accrual rate. In short, the Plan's cash balance formula provides participants the same declining rate of benefit accrual based on age as would a traditional defined benefit plan that simply stated in its text the above accrual rates without any formula to disguise the effect.

3. As part of the 1999 conversion to the cash balance formula, IBM chose to provide a one-time unearned accrued benefit, the Always Cash Balance enhancement (ACBE), to younger employees based solely on age. To implement the instant accrual of this benefit for younger workers, IBM used a "comparison formula" to determine the hypothetical dollar amount of each employee's opening PPAcct. CA App. 268-269, § 17.5(b); *Id.*, 391.

The results produced by the ACBE depended entirely on an employee's age as of June 30, 1999, the day before the plan conversion. For employees under a certain age (about 42), the ACBE provided a larger amount – up to twice as much – than the present value of their existing benefit. For older employees, the present value of their existing benefit exceeded the ACBE amount, so the conversion formula provided them no additional benefit solely because of their age. Thus, younger employees received an instantaneous increase in their pension benefit while older workers received no increase at all. CA Supp. App. 87. The following chart demonstrates the discriminatory treatment of an older employee compared to a younger employee with the same salary and service history (derived from CA App. 434, 438-439):

| Line# | | | |
|---|---|---|---|
| 1 | Age at 6/30/99 | 38 | 46 |
| 2 | Service at 6/30/99 | 9 | 9 |
| 9 | Age 65 Annuity at 6/30/99 | 7,140 | 7,041 |
| 14 | Present Value Formula at 7/1/99 | 15,762 | 24,775 |
| 15 | ACBE at 7/1/99 | 19,757 | 19,757 |
| | ACBE Increase in Opening Balance [15-14] | 3,995 | 0 |
| 26 | CB Age 65 Annuity at 7/1/99 | 7,572 | 6,187 |
| | ACBE Increase in Age 65 Annuity [26-9] | 432 | 0 |

IBM management understood that these differences in additional benefits depended entirely upon employees' ages on June 30, 1999. In a May 4, 1999, e-mail to senior IBM managers, the Plan's enrolled actuary explained that:

> Due to the nature of the IBM Retirement Plan vs. the Personal Pension Account, younger employees will benefit the most from this Always Cash Balance enhancement. On average, very young employees (in their 20's), could see their benefit double due to the enhancement, while a person who is in their early 40's might only see a 10% increase due to the Always Cash Balance enhancement. Older employees (over 45) will generally not be covered by the Always Cash Balance enhancement. CA Supp. App. 87.

He concluded that "[a]s you can see, the excess percentage of the ACB over the basic opening account balance is directly related to age." *Id.*, 88.

This gratuitous benefit increase for younger employees affected both the amount of the immediate benefit to which employees were entitled as a lump-sum distribution and, to an even greater extent, the age-65 accrued benefit derived from that opening account balance projected

forward to normal retirement age at the Plan's interest crediting rate. Thus, participants who received the ACBE and terminated employment on July 1, 1999, would have received accrued benefits significantly higher (as much as double) what they were entitled to the day before.

4. The district court concluded that under IBM's cash balance formula, the rate of an employee's benefit accrual was reduced every year because of the increase in his age, in violation of ERISA Section 204(b)(1)(H)(i). App. 32-37. The district court also ruled that the ACBE violated ERISA Section 204(b)(1)(H)(i) because it provided an immediate accrual of unearned benefits for younger employees but no increase for older workers solely based on the employee's age. App. 42-43. The parties then settled all other issues, including increased benefits for the class, and the district court entered judgment. App. 42-44. The monetary relief awarded to the class with respect to the two issues raised by this Petition totals $1.4 billion in increased benefits.

5. The Seventh Circuit reversed on both issues. App. 1-13. Writing for the court, Judge Easterbrook concluded that cash balance plans are functionally equivalent, in economic terms, to defined contribution plans and should be governed by the same age discrimination principles as defined contribution plans. App. 1-2. Judge Easterbrook also ruled that, despite the different statutory terms used by Congress, ERISA's prohibition of age discrimination in defined benefit plans was essentially identical to the provision governing age discrimination in defined contribution plans. App. 3-5. Consequently, he opined that the cash balance formula did not violate ERISA because it provided that the employer would make hypothetical annual pay credit "contributions" to employees' hypothetical accounts at an equal rate regardless of an employee's age, even though those contributions resulted in higher benefits for younger employees at normal retirement age. The opinion attributed the higher benefits provided to younger workers to the "time value of money" rather than age discrimination because younger workers could wait

longer than older workers to receive their benefits. App. 4-6.

With respect to the Always Cash Balance Enhancement provided to younger but not older workers, Judge Easterbrook similarly held that there was no impermissible age discrimination under ERISA. Judge Easterbrook contended that older workers did not lose any benefits because of age just because younger workers are given an additional economic benefit. He further asserted that younger workers can properly be granted a gratuitous benefit increase denied to older workers. App. 12.

## REASONS FOR GRANTING THE WRIT

It is axiomatic that it is not the role of the federal judiciary in statutory construction to second guess the wisdom of the policy judgments made by Congress. Yet, that is precisely what the Seventh Circuit, through Judge Easterbrook's opinion, did in this case. Based on Judge Easterbrook's preferred economic theory of what should and should not constitute impermissible age discrimination, the appellate court determined that it was sound economic policy for respondents to adopt a pension plan that indisputably provides lower benefits to older employees than to younger employees because of their age. Congress, however, made a very different policy choice in ERISA by expressly barring pension plans from drawing that very distinction based on age. And, notwithstanding the lower court's Herculean efforts to twist the plain meaning of the statutory language to create an exemption from ERISA's nondiscrimination mandate, the statutory language Congress actually enacted admits of no such exception.

As described below, the Seventh Circuit's improper substitution of its own policy views for those of Congress resulted in its upholding two distinct aspects of respondents' pension plan: the cash balance formula and its method of assigning initial benefits to older and younger employees. Both rulings are legally erroneous. The first

error, however, is the more far-reaching because it conflicts with decisions of three other circuits and potentially affects millions of employees, even beyond the more than 250,000 directly implicated in this case. Although the second issue is more case specific, we urge the Court to grant both issues in the event that the Court grants the first issue. Granting both would be proper because the lower court treated its resolution of the first issue as effectively dispositive of the second, and resolving both issues is required to provide full relief to petitioners. The second issue also presents a distinct circuit conflict.

## I. REVIEW IS WARRANTED OF THE SEVENTH CIRCUIT'S ERRONEOUS CONCLUSION THAT RESPONDENTS' DEFINED BENEFIT PENSION PLAN DOES NOT VIOLATE ERISA'S PROHIBITION AGAINST AGE DISCRIMINATION.

IBM's pension plan plainly discriminates on the basis of age. The employee's rate of benefit accrual based on a single year's work depends not just on salary, but also on age. The formula is both straightforward and quite simple: the older the employee, the lower the rate of benefit accrual for that year even if two employees are otherwise being paid the same annual salary. In short, the pension plan treats younger employees more favorably than older ones precisely because they are younger.

ERISA forbids that result in defined-benefit plans. The statute provides that it constitutes unlawful age discrimination if "the rate of an employee's benefit accrual is reduced, because of the attainment of any age." 29 U.S.C. § 1054(b)(1)(H)(i). The Seventh Circuit reached the contrary result only by substituting its view of impermissible age discrimination for that supplied by Congress in ERISA. Concluding that the cause of the discriminatory treatment was merely the "time value of money" that

naturally inured to the benefit of those with more time until reaching normal retirement age (*i.e.*, those who are younger), Judge Easterbrook determined that Congress did not intend to prohibit it. App. 5-6. Thus persuaded, Judge Easterbrook was not deterred by the plain meaning of the actual statutory language, which does not include even the barest suggestion of the policy exception to age discrimination created by the court below.

Review by this Court is warranted not just because the lower court's ruling is legally erroneous, but also because Judge Easterbrook's reasoning conflicts with rulings of three other circuit courts and because of the ruling's extraordinarily far reaching implications. Literally millions of workers are subject to pension plans similar to that at issue in this case and the Seventh Circuit's misapplication of ERISA's nondiscrimination mandate threatens to deprive them of its essential protection.

### A. The Seventh Circuit Ignored the Plain Meaning of ERISA's Test for Impermissible Age Discrimination.

The Seventh Circuit committed two distinct errors in reaching its conclusion that respondents' defined-benefit pension plan does not violate ERISA's prohibition of age discrimination. First, the court wrongly equated the economics of a defined benefit plan that uses a cash balance formula with a defined contribution plan. Second, the court inappropriately narrowed the congressional test for impermissible age discrimination applicable to defined benefit plans by misconstruing the term "employee's rate of benefit accrual" to mean the "employer's rate of contribution," which has an entirely different meaning and regulatory focus.

### 1. A Defined Benefit Plan Using a Cash Balance Formula Is Not Economically Equivalent to a Defined Contribution Plan.

The court of appeals found that IBM's cash balance formula was not age discriminatory by treating it as a defined contribution plan and applying the equal annual contribution test applicable to defined contribution plans. App. 1-5. Judge Easterbrook's opinion failed to recognize that ERISA's distinctly different rules prohibiting age discrimination in defined contribution and defined benefit plans follow from the fundamental economic differences between the two types of plans. Those basic differences are reflected in Congress's use of different definitions of "accrued benefit" in defined contribution and defined benefit plans. As *Hughes Aircraft* explained, "accrued benefit" in a defined contribution plan is simply "the balance of the individual's account." ERISA § 3(23)(B), 29 U.S.C. § 1002(23)(B). Consequently, age discrimination occurs in defined contribution plans if "the rate at which amounts are allocated to employee's account is . . . reduced, because of the attainment of any age." ERISA Section 204(b)(2)(A), 29 U.S.C. § 1054(b)((2)(A).

By contrast, in defined benefit plans the "employee's accrued benefit" is "expressed in the form of an annual benefit commencing at normal retirement age." ERISA § 3(23)(A), 29 U.S.C. § 1002(23)(A). Consequently, the test for age discrimination provided in ERISA Section 204(b)(1)(H)(i) is whether "the rate of an employee's benefit accrual is reduced, because of the attainment of any age." This test focuses on the amount of benefits the employee will receive beginning at normal retirement age, and there is no testing of "contributions" because there

are none to test. Hence the term "defined *benefit* plan": the employer makes no current contributions of funds to specific individual employee accounts, as would be the case under a defined contribution plan, but instead funds the pension plan on a group basis, makes the investment decisions, takes the investment risk, and is obligated to pay an amount of benefits at normal retirement age determined by a formula based on compensation and service years, not on the amount of the employer's funding of the plan. While cash balance plans are designed to superficially resemble defined contribution plans, it is well settled that they make the same promise to pay a specific benefit upon retirement in the same manner as any other defined benefit plan. Thus, they are governed by the same ERISA provisions as traditional defined benefit plans, *Esden*, 229 F.3d at 158, and as noted there are no "contributions" or "accounts" to test, only a formula that guarantees a retirement benefit.

Nevertheless, the Seventh Circuit treated IBM's cash balance plan as "economically equivalent" to a defined contribution plan and held that the "benefit accrual" in a cash balance plan can be tested in terms of an assumed, but not real, pay credit the employer "contributes" each year to the hypothetical cash balance account rather than the employee's actual entitlement under a cash balance formula, which is the "benefit under the plan commencing at normal retirement age." However, the fundamental differences between such plans – in terms of both investment risk and entitlement to investment gain – conclusively demonstrate that the Seventh Circuit is wrong. A defined benefit plan using a cash balance formula and a defined contribution plan are not "materially equivalent." Zelinsky Cooper Critique 23. In a defined benefit plan using a cash balance formula – completely unlike a defined contribution plan – "the employee covered by his

employer's cash balance plan, for better or worse, receives a fixed promise which shifts funding and investment risk to the employer." *Id.* at 21.

Having ignored the carefully crafted statutory differences between defined benefit and defined contribution plans, the Seventh Circuit expressly approved (App. 4-5) IBM's plan design that provides an annual accrual equal to 3% of salary for a 25-year-old participant which steadily declines with age to .4% of salary for an otherwise similarly situated 65-year-old. As IBM fully admitted (IBM 7th Cir. Reply Br. 14), a traditional defined benefit plan that provided such a declining rate of benefit accrual would violate ERISA Section 204(b)(1)(H)(i). Despite that admission, the Seventh Circuit excused IBM's cash balance formula – which provides precisely the same declining rate of benefit accrual as the admittedly discriminatory traditional plan – because those accrual rates purportedly result from compounding fictional interest credits to a fictional account. This exalts form over substance. If a traditional defined benefit plan cannot provide such a rate of benefit accrual, then a cash balance formula cannot be permitted to do so based on hypothetical "interest credits" "earned" on a non-existent account.

### 2. Judge Easterbrook's Opinion Misconstrued the Term "Employee's Rate of Benefit Accrual" To Mean "Employer's Rate of Contribution."

In addition to equating the cash balance formula to a defined contribution plan in economic terms, the Seventh Circuit held that "there is no statutory difference between the treatment of economically equivalent defined-benefit and defined-contribution plans." App. 5. The court purportedly found equivalence in the two standards of age discriminatio - ERISA § 204(b)(1)(H)(i) for defined

benefit plans and § 204(b)(2)(A) for defined contribution plans – by comparing them side-by-side. App. 3.

While Judge Easterbrook, without textual analysis, concluded that they "appear to say the same thing," (App. 3), the two standards are quite different because they reflect the fundamental differences between defined contribution and defined benefit plans. For defined benefit plans, including those using a cash balance formula, Section 204(b)(1)(H)(i) provides that "the rate of an employee's benefit accrual" cannot permissibly be "reduced, because of the attainment of any age." For defined contribution plans, Section 204(b)(2) provides that "the rate at which amounts are allocated to the employee's account" cannot permissibly be "reduced, because of the attainment of any age." Judge Easterbrook's opinion distorts the normal meanings of "allocate" and "benefit accrual." First, "[i]f these provisions say the same thing, why did the draftsmen write and Congress add to the [Internal Revenue] Code, ERISA and ADEA two different provisions addressing pension plan discrimination?" Zelinsky Cooper Critique 24. Professor Zelinsky points out that throughout ERISA, whenever a single rule applies to both defined benefit and defined contribution plans, only one statutory provision is provided. When separate policies apply to each type of plan, two statutory provisions are provided. *Id.* at 24-25. Here, Congress used strikingly different terms in each provision which follow from the fundamental differences in the two types of plan:

> [I]f the draftsmen who wrote the pension age discrimination statutes and the Congress which added them to the Code and ERISA meant to say "contribution," why instead did they say "benefit accrual?" More convincingly, "contribution" means "contribution" and "benefit accrual" pertains to the accrual of benefits under defined benefit plans. *Id.* at 26-27.

As Judge Baer in the Southern District of New York recently ruled in refusing to follow *Cooper*:

> The fact is accrual, using its dictionary meaning and in line with the structure of defined benefit plans, refers to what the employee accumulates (the outputs from the plan) whereas allocation, using its dictionary definition and in line with the structure of defined contribution plans, refers to what an employer puts into the account.

*In re J.P. Morgan Chase Cash Balance Litigation*, 2006 WL 2063424 at *9 (S.D.N.Y. Oct. 30, 2006).

Hence, Judge Easterbrook's use of the defined contribution standard for age discrimination to legitimize the declining rate of benefit accrual in cash balance plans is refuted both by the fundamental economic differences between such plans and the starkly different legal standards for age discrimination in defined benefit and defined contribution plans.[3]

Finally, the court's misconstruction of the meaning of "benefit accrual" prompted its further error in concluding that respondents' plan merely reflects the "time value of money" rather than impermissible age discrimination. In the striking absence of any statutory or case law

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[3] Indeed, Judge Easterbrook's reliance on hypothetical contributions to a non-existent account contradicts the IBM Plan's own description of the cash balance account:

> The Personal Pension Account shall be a recordkeeping account only, and neither the maintenance of, nor the crediting of amounts to, such Personal Pension Account shall be treated as an allocation of assets of the Plan, or a segregation of such assets in, any such Personal Pension Account. A Personal Pension Account shall not create any right for any person to receive specific assets of the Plan. CA App. 242, § 11.2(b).

authority,[4] the court asserted that the younger employees' higher benefit accrual rate compared to older employees with the same service and salary history should not be considered unlawful because it was justified by the longer time that younger employees wait to receive their benefits. App. 4-6.

But Judge Easterbrook's creation of a statutory exception because of the time value of money contradicts the express terms of Section 204(b)(1)(H)(i), which prohibits the reduction of "the rate of an employee's benefit accrual ... because of the attainment of any age." To establish a violation, this Section requires only that *any* employee's rate of benefit accrual decreases with age. It is indisputable that *every* participant in IBM's Plan will experience a reduction in the benefit accrual rate with increasing age. That is established by the table on page 9 above. Applying the "time value of money" does not change the mathematics of discriminatory benefit accrual.

[4] No doubt because of the absence of any applicable legal authority, the lower court ultimately resorted (App. 6-7) to a quotation from the preamble to proposed Treasury Department regulations that were *withdrawn* in response to an express Congressional mandate arising from concerns that the regulations might adversely impact the District Court's decision in this case. *See* Section 205, Consolidated Appropriations Act of 2004, P.L. 108-109. Judge Easterbrook somehow equates that preamble language as the legal equivalent of the views of the Treasury Department.

### B. The Seventh Circuit's Decision Conflicts with Decisions of the Second, Ninth, and Eleventh Circuits.

The linchpin of Judge Easterbrook's opinion is his treating each employee's current cash balance account as the baseline for determining age discrimination in the rate of benefit accrual. Only by assuming the existence of actual annual contributions to an existing account balance could he eliminate from his legal analysis the future value of the "interest credits" that must be included in an employee's hypothetical account and therefore hold that the amount being "input" by IBM each year does not discriminate against older workers.

Every other court of appeals that has considered this issue has flatly rejected Judge Easterbrook's reasoning, which is essential to the Seventh Circuit's ruling. The Second Circuit in *Esden,* 229 F.3d at 162-164, the Ninth Circuit in *Miller v. Xerox Corp. Retirement Income Guarantee Plan*, 464 F.3d 871, 875-877 (9th Cir. 2006), and the Eleventh Circuit in *Lyons v. Georgia-Pacific Corp. Salaried Employees Ret. Plan*, 221 F.3d 1235, 1251-1252 (11th Cir. 2000), *cert. denied*, 532 U.S. 967 (2001), held that the current account balance must be ignored in analyzing defined benefit plans using the cash balance formula because that current account balance is purely hypothetical. An employee participating in a defined benefit plan using a cash balance formula is entitled, as in any defined benefit plan, to an accrued benefit at normal retirement age, and the measuring rod for violations of the employee's rights under ERISA is that accrued benefit, not a fictional account balance.

This conflict arises from a fundamental disagreement concerning the nature of an employee's accrued benefit in a defined benefit plan using a cash balance formula. In *Esden*, Judge Pierre Leval, writing for the Second Circuit,

held that "the accrued benefit under a defined benefit plan must be valued in terms of the annuity that it will yield at normal retirement age." 229 F.3d at 163. As a result, to determine an employee's accrued benefit in a cash balance plan, the current account balance must be projected to normal retirement age by adding the hypothetical "interest credits" for each year through normal retirement age. *Id.* at 165-166.

The Eleventh Circuit in *Lyons* addressed the same issue concerning the nature of the employee's accrued benefit in a cash balance plan and similarly held that the employee's accrued benefit was not the amount in his hypothetical account. 221 F.3d at 1251. Instead, for each year of service the employee "earned a vested interest in an amount at normal retirement age, to be calculated under the Plan by projecting forward the amount in his hypothetical account using the interest credit rates specified in the Plan." *Id.*

Judge Easterbrook flatly rejected these holdings: "Nothing in either ERISA or the IBM plan requires 40 years of interest to be credited to the account as soon as the younger worker earns wages." App. 8.

In *Esden*, Judge Leval not only described the "regulatory consequences" of the differing plan classifications as "wide reaching," but further singled out as primary consequences the differing definitions of "accrued benefit" applicable to each kind of plan and that "defined benefit plans are subject to a series of parallel statutory constraints . . . from which defined contribution plans are exempted." *Id.* at 158-59. And, in sharp contrast to the Seventh Circuit, the Second Circuit expressly recognized the legal significance under ERISA of the defining characteristic of a cash balance plan that justifies its regulatory treatment as a defined benefit plan: "the individual accounts, and the employer contributions and the interest credits to those accounts, are all hypothetical." *Id.* at 159, n.6. The Second Circuit, accordingly, rejected Judge

Easterbrook's central justification for the Seventh Circuit's ruling in this case, that the hypothetical nature of a cash balance plan could be assumed away and be treated under ERISA as the legal equivalent of a defined contribution plan with actual annual contributions.

The Ninth Circuit's decision in *Miller* likewise conflicts with the Seventh Circuit's ruling in this case. At issue in *Miller* was whether a procedure used by Xerox Corporation to reduce pension benefits at final retirement to account for earlier benefit distributions violated ERISA. In concluding that the pension plan violated ERISA, the Ninth Circuit, like the Second Circuit in *Esden* and the Eleventh Circuit in *Lyons*, accounted for ERISA's differing regulatory treatment of defined benefit and defined contribution plans, including the hypothetical nature of the employer's annual contributions. The Ninth Circuit specifically declined to analyze the validity of the pension plan at issue in *Miller* based on the plan operator's contention that it could fairly be equated to a defined contribution plan under which actual annual contributions were being made: "In short, Xerox may not use a projected-to-the-present value generated from a phantom account as a proxy for the actual distribution amount." *Id.* at 876.

Unlike the decision below, *Esden*, *Lyons*, and *Miller* did not decide an age discrimination claim under ERISA. But that distinction does not diminish or otherwise undermine the existence of a circuit conflict. Just the opposite. It both underscores the existence of a circuit conflict and magnifies its consequences. As *Esden*, *Lyons*, and *Miller* make clear, the legal consequences of the Seventh Circuit's error are not confined to ERISA age discrimination claims. A failure to respect ERISA's essential distinction between defined benefit plans and defined contribution plans, including defined benefit plans that purport to mimic features of a defined contribution plan, affects a wide range of regulatory consequences under

ERISA. ERISA's prohibition against age discrimination is just one example of those consequences.

Nor is there any room for doubt that the existing circuit conflict over the broader legal issue of the regulatory treatment under ERISA of defined benefit plans with cash balance formulas will inexorably lead to an even squarer circuit conflict in applying ERISA's nondiscrimination mandate. This conflict over the propriety of using the current account balance in a cash balance formula to define the participant's accrued benefit dictates whether a cash balance formula will be held to violate Section 204(b)(1)(H)(i). If the measuring rod is the employee's accrued benefit at normal retirement age, then it is indisputable that the employee's rate of benefit accrual under a cash balance formula declines with age in violation of Section 204(b)(1)(H)(i).

Indeed, the existing conflict in the circuits created by the Seventh Circuit ruling has already resulted in sharply differing district court decisions on the ERISA age discrimination issue, in just the few months since the Seventh Circuit's ruling. Two district courts in the Second Circuit recently rejected Judge Easterbrook's analysis and instead, following *Esden*, held that the cash balance account is irrelevant and therefore the cash balance formula violates Section 204(b)(1)(H)(i) because it results in a benefit accrual rate that decreases with age.[5]

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[5] *In re J.P. Morgan Chase Cash Balance Litigation*, 2006 WL 3063424 at *9 (S.D.N.Y. Oct. 30, 2006); *Richards v. FleetBoston Financial Corp.*, 2006 WL 3000768 at *3 (D. Conn. Oct. 16, 2006), refusing to reconsider its original ruling in favor of plaintiff, *Richards v. FleetBoston Financial Corp.*, 427 F. Supp. 2d 150 (D. Conn. 2006), in light of the Seventh Circuit's decision in this case. *But see Laurent v. PriceWaterhouseCoopers LLP*, 448 F. Supp. 2d 537, 2006 WL 2546805 at *11-15 (S.D.N.Y. Sept. 5, 2006) (adopting the Seventh Circuit's reasoning). There are at least three other active cases in which district courts

(Continued on following page)

Finally, the existence of the pending lower court age discrimination cases does not support this Court's awaiting their resolution on further appeal. The national stakes here are too high for this Court to wait until other circuits decide the specific Section 204(b)(1)(H)(i) issue presented by this case. The existing circuit conflict is not restricted to the age discrimination context, which is only one of many regulatory consequences affected, but instead simply underscored by it. And, apart from the obvious national interest in this Court's addressing the broad legal issue that is the subject of the existing circuit conflict, there are compelling equitable reasons raised just in this case that counsel against further delay. If this petition is denied, more than 250,000 IBM Plan participants will permanently lose their right to compensation in excess of $1 billion for unlawful age discrimination even if this Court ultimately determines, consistent with the reasoning of the Second, Eleventh, and Ninth Circuits, that the cash balance formula violates Section 204(b)(1)(H)(i). Participants in other plans will suffer the same permanent loss if their claims are rejected and they exhaust appellate review before this Court decides these issues.

The legal questions raised by the cash balance formula have been fully developed in this case, and no further refinement will be gained by delaying this Court's intervention. These issues are solely legal in nature and do not turn on factual matters. Thus there is no reason to suppose that a future case will provide this Court with a better or cleaner record than this one.

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rejected age discrimination claims against cash balance plans. *See Register v. PNC Fin. Servs. Group, Inc.*, 2005 WL 3120268 (E.D. Pa. Nov. 21, 2005), *appeal pending*, 3d Cir. No. 05-5445; *Hirt v. Equitable Retirement Plan*, 441 F. Supp. 2d 516 (S.D.N.Y. 2006); *Drutis v. Quebecor World (USA), Inc.*, 2006 U.S. Dist. LEXIS 84950 at *16-20 (E.D. Ky. Sept. 25, 2006), *appeal pending*, No. 06-6380 (6th Cir.).

### C. The Legal Issues Presented by this Case Are Important.

The cash balance formula is currently used by many major American corporations to define what pensions their defined benefit plans will provide to over eight million workers. The proponents of cash balance plans have known since the formula's inception that it provides lower pension benefit accruals for older workers. Indeed, that is one of the formula's principal goals: to make the cost of providing older employees' pensions equal to the cost of providing pensions to younger workers by reducing the dollar value of the older worker's retirement annuity as compared to the dollar value of a younger worker's annuity. To mask this reduction, the cash balance formula pretends to be a 401k plan and attempts to focus the analysis away from the retirement annuity and onto a hypothetical "account balance." The issue in this case is whether the legal requirements ERISA imposes on defined benefit plans can be excused simply because the cash balance formula has superficial similarities to a 401k plan (which, as a defined contribution plan, is not subject to the same rules).

In the Pension Protection Act of 2006 ("PPA"), Congress refused to retroactively legitimize use of the cash balance formula and did so prospectively only with safeguards absent from the IBM Plan.[6] Consequently, the PPA

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[6] The PPA added protections for older employees when a plan converts to a cash balance format, including a shorter three-year vesting period, specifying the interest rate to be used to determine a participant's annuity at normal retirement age in the event of plan termination, and requiring that a participants' opening account balances be at least equal to their accrued benefits under existing plan at the date of conversion. P.L. 109-280, § 701. IBM's Plan does not satisfy all the new statutory requirements and therefore does not qualify prospectively as a valid cash balance plan.

did not affect the rights of millions of employees, including more than 250,000 in this case, to recover benefits lost because of age discrimination. Wholly apart from the prospective operation of the PPA, those interests are sufficiently great to warrant this Court's review, rather than allow for their resolution to turn on the happenstance whether the relevant employer falls within the jurisdiction of one federal circuit rather than another.

## II. THE SIXTH AND SEVENTH CIRCUITS CONFLICT ON THE LEGALITY OF BENEFIT INCREASES PROVIDED ONLY TO YOUNGER EMPLOYEES.

The Seventh Circuit committed a second legal error as well. In a discussion limited to a single paragraph, the court (App. 12) dismissed petitioners' challenge to the Always Cash Balance Enhancement as a "rehash" of their contention that IBM's cash balance plan violated ERISA Section 204(b)(1)(H)(i). That is incorrect. In fact, the ACBE would unquestionably be illegal under the Seventh Circuit's "equal contribution" test: IBM made extra contributions to younger employees' opening account balances, while older employees' opening accounts were limited to their vested benefits under the prior plan. As a result of these unearned inputs, younger employees' retirement benefits instantly became larger than under the prior plan, while older worker's benefits remained unchanged. IBM's management was fully advised by the Plan's enrolled actuary of this discriminatory effect: "As you can see, the excess percentage of the ACB over the basic opening balance is directly related to age. Young employees get the benefit of the ACB and old participants do not." CA Supp. App. 88.

Judge Easterbrook's only legal justification for these age-based benefit differences is that "[a]n employer is free

to move from one legal plan to another legal plan, provided that it does not diminish vested interests – and this transition did not." App. 12. Without citing any supporting authority, the Seventh Circuit held that an employer, when changing plan designs, may increase only younger workers' benefits as long as older workers' vested benefits are not decreased.

This sweeping holding conflicts with the Sixth Circuit's decision in *EEOC v. Jefferson County Sheriff's Dept.*, 467 F.3d 571 (6th Cir. 2006) (*en banc*). The plan in that case provided that employees in hazardous positions disabled after age 55 or 20 years of service received their normal retirement benefits for which they were eligible at age 55 or after 20 years of service. However, disabled employees younger than 55 were credited with additional years of service to provide the benefits they would have received if they had worked to age 55 or reached 20 years of service. These terms resulted in some younger employees receiving greater benefits than older employees based on the same actual service and salary history. In adopting this plan for state and county employees, Kentucky did not take vested benefits away from the older workers, but the Sixth Circuit nevertheless ruled that the plan illegally discriminated against older employees. *Id.* at 579-580.

This Court should resolve this conflict by reversing the Seventh Circuit's approval of pension benefit increases limited to younger employees.

## CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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NOVEMBER 28, 2006

**Kathi COOPER, et al., on behalf of a class, Plaintiffs-Appellees,**

**v.**

**IBM PERSONAL PENSION PLAN and IBM CORPORATION, Defendants-Appellants.**

**No. 05-3588.**

United States Court of Appeals, Seventh Circuit.

Argued Feb. 16, 2006.

Decided Aug. 7, 2006.

Rehearing and Rehearing En Banc Denied Sept. 1, 2006.*

Lee A. Freeman, Jr. (argued), Freeman, Freeman & Salzman, Chicago, IL, for Plaintiffs-Appellees.

Jeffrey G. Huvelle (argued), Covington & Burling, Washington, DC, for Defendants-Appellants.

Kent A. Mason, Davis & Harman, Washington, DC, for Amicus Curiae.

Before BAUER, EASTERBROOK, and MANION, Circuit Judges.

EASTERBROOK, Circuit Judge.

The IBM Personal Pension Plan is a cash-balance defined-benefit plan. It is almost, but not quite, a defined-contribution plan. Although each employee in a

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* Circuit Judges Kenneth F. Ripple, Ilana Diamond Rovner and Ann Claire Williams took no part in the consideration of this matter.

defined-contribution plan has a fully funded individual account, the personal account in a cash-balance plan is not separately funded. Instead IBM imputes value to the account in the form of "credits": there are pay credits (set at 5% of the employee's gross taxable income) and interest credits (set at 100 basis points above the rate of interest on one-year Treasury bills). A trust holds assets that may (or may not) be enough to fund all of the individual accounts when workers quit or retire. IBM's plan permits an employee who quits or retires after working long enough for pension benefits to vest (a maximum of five years) to withdraw the balance in cash or roll it over into a fully funded annuity. During the time before cash-out the employee takes the risk that IBM will suffer business reverses and be unable to pay the full stated value of the account (if the amount already in trust for participants as a group turns out to be insufficient); otherwise IBM's plan is economically identical to a defined-contribution plan funded the same way and invested in a bond fund that returns 1% above the Treasury rate.

Plaintiffs in this class-action litigation contend that IBM's plan violates a subsection of ERISA (the Employee Retirement Income Security Act) that prohibits age discrimination. The district court ruled in plaintiffs' favor, see 274 F.Supp.2d 1010 (S.D.Ill.2003), and proceedings continued as the parties debated how much IBM owes (and how it must change its plan in future years) as a remedy. That subject has been resolved to mutual satisfaction – contingent on the district judge being right on the merits – so this appeal is limited to the question whether the plan is unlawfully discriminatory.

All terms of IBM's plan are age-neutral. Every covered employee receives the same 5% pay credit and the same

interest credit per annum. The basis of the plaintiffs' challenge – and the district court's holding – is that younger employees receive interest credits for more years. The language on which plaintiffs rely was added to ERISA in 1986; Congress also enacted a parallel provision covering defined-contribution plans. Pub.L. 99-509, 100 Stat. 1874, 1975, 1976 (1986). We set these out alongside to facilitate comparison:

| Defined-benefit plans: ERISA § 204(b)(1)(H)(i), 29 U.S.C. § 1054(b)(1)(H)(i) | Defined-contribution plans: ERISA § 204(b)(2)(A), 29 U.S.C. § 1054(b)(2)(A) |
|---|---|
| [A] defined benefit plan shall be treated as not satisfying the requirements of this paragraph if, under the plan, an employee's benefit accrual is ceased, or the rate of an employee's benefit accrual is reduced, because of the attainment of any age. | A defined contribution plan satisfies the requirements of this paragraph if, under the plan, allocations to the employee's account are not ceased, and the rate at which amounts are allocated to the employee's account is not reduced, because of the attainment of any age. |

These appear to say the same thing, except that the rule for defined-benefit plans tells us what is not allowed, while the rule for defined-contribution plans tells us what works. Either way, the employer can't stop making allocations (or accruals) to the plan or change their rate on account of age. The IBM plan does neither of these things and therefore, one would suppose, complies with the statute. If this were a real, rather than a phantom, defined-contribution plan, that much would be taken for granted. Yet if the 5%-plus-interest formula is non-discriminatory when used in a

defined-contribution plan, why should it become unlawful because the account balances are book entries rather than cash?

Plaintiffs persuaded the district court, however, that the two subsections are radically different. That difference is attributable to the phrase "benefit accrual," which appears in the subsection for defined-benefit plans but not the one for defined-contribution plans. Neither ERISA nor any regulation defines this phrase, so the district judge went looking for some equivalent elsewhere in the statute. It found the phrase "accrued benefit," which is defined in § 3(23)(A), 29 U.S.C. § 1002(23)(A). An "accrued benefit" is an amount "expressed in the form of an annual benefit commencing at normal retirement age." Plug this back into § 204(b)(1)(H)(i), and the rule against discrimination then refers not to what IBM puts into the plan, but what the employee takes out on retirement. Someone who leaves IBM at age 50, after 20 years of service, will have a larger annual benefit at 65 than someone whose 20 years of service conclude with retirement at age 65. The former receives 15 years' more interest than the latter – and the judge assumed that this is not counterbalanced by the fact that older workers generally draw higher salaries. Under the district court's analysis, compound interest becomes a scourge, for the younger the employee when any given year's salary is earned, the greater the payout "expressed in the form of an annual benefit commencing at normal retirement age."

This approach treats the time value of money as age discrimination. Yet the statute does not require that equation. Interest is not treated as age discrimination for a defined-contribution plan, and the fact that these subsections are so close in both function and expression

implies that it should not be treated as discriminatory for a defined-benefit plan either. The phrase "benefit accrual" reads most naturally as a reference to what the employer puts in (either in absolute terms or as a rate of change), while the defined phrase "accrued benefit" refers to outputs after compounding. That's where this litigation went off the rails: a phrase dealing with inputs was misunderstood to refer to outputs. As long as we think of "benefit accrual" as referring to what the employer imputes to the account – an understanding reinforced by the use of the word "allocation" in the subsection addressing defined-contribution plans – there is no statutory difference between the treatment of economically equivalent defined-benefit and defined-contribution plans. For defined-benefit plans, where the account is an accounting entry rather than cash, "benefit accrual" matches the money "allocated" to a defined-contribution plan.

Nothing in the language or background of § 204(b)(1)(H)(i) suggests that Congress set out to legislate against the fact that younger workers have (statistically) more time left before retirement, and thus a greater opportunity to earn interest on each year's retirement savings. Treating the time value of money as a form of discrimination is not sensible. Cf. *Hazen Paper Co. v. Biggins*, 507 U.S. 604, 611, 113 S.Ct. 1701, 123 L.Ed.2d 338 (1993) (variables correlated with age must be kept "analytically distinct" from age when searching for discrimination). The parallel between the subsections for defined-benefit and defined-contribution plans shows as much. All sorts of things go wrong unless we treat both § 204(b)(1)(H)(i) and § 204(b)(2)(A) as addressing the rate at which value is added (or imputed) to an account, rather than the annual pension at retirement age. Consider a formula that adds

$500 to annual pension benefits for every year worked. This setup economically favors older workers (as does a top-five-year-salary multiplier) because it ignores the time value of money and treats the last year of work as contributing equally with the first. Yet on the plaintiffs' understanding it would be a form of discrimination against the old, because the $500 is a smaller "rate of benefit accrual" as time passes. Someone who worked two years would get a "100% rate of increase" in his second year (his annual benefits on retirement would jump from $500 to $1,000), while someone who works 20 years receives only a 2.56% increase (from $19,500 to $20,000) in Year 20.

Our conclusion that "benefit accrual" (for defined-benefit plans) and "allocation" (for defined-contribution plans) both refer to the employer's contribution rather than the time value of money between contribution and retirement has the support of regulations that the Treasury Department proposed. (Appropriations riders have prevented the Treasury from taking final action on the draft regulations, but they still help to inform our understanding of the statute.) The draft regulations treat the "rate of benefit accrual" as "the increase in the participant's accrued normal retirement benefit for the year." 67 Fed.Reg. 76123, 76125 (Dec. 11, 2002). For cash-balance plans in particular the phrase would have been defined as "the additions to the participant's hypothetical account for the plan year." 67 Fed.Reg. at 76126. The draft specifies that interest credits must accrue "at a reasonable rate of interest that does not decrease because of the attainment of age" and be provided "for all future periods, including after normal retirement age." *Ibid.*

Thus the Treasury's view, like our independent reading, looks at the rate of contribution (what goes into the

account) rather than the annual rate of withdrawal at retirement. The Treasury asks: "if this employee were younger, would the hypothetical balance have grown more this year?" For IBM's plan, the answer is no. When an employee is 20, his account is increased monthly by 5% of his salary plus credits based on the account's balance multiplied by a prescribed interest rate. The same is true when the employee turns 50, 60, or 70. Neither the contribution rate nor the interest rate changes with age. (No one contests the rate at which interest is credited – though 100 basis points over the Treasury rate looks low compared with what investments could earn in the private market and therefore could be understood to disfavor younger employees.)

Plaintiffs propose a different definition of "benefit accrual": annual pension (at retirement age) divided by salary. Contributions at age 25 produce an annual pension benefit that equals about 3% of each year's income in nominal dollars, while contributions at 65 produce annual benefits only 0.4% of the year's income. Not surprising, and hardly illuminating; this is just another illustration of the power of compound interest. The example depends on (a) allowing the pension to be increased by compounding, while (b) failing to discount the pension to present value. Stated another way, this example compares 1966 dollars (when the 25-year-old earned the salary) with 2006 dollars (when that person turns 65 and starts to draw a pension); of course the return on investment looks good, but much of it is inflation and the rest is real interest rates. The person who earns a salary in 2005 and retires in 2006 is (materially) unaffected by both inflation and compound interest. Nothing depends on age. Someone who earns a salary at age 65 and waits 40 years to start drawing a pension

would receive the same 3%-of-salary-per-retirement-year as the illustrative 25-year-old who retires at 65; and someone who earns wages at 25 and retires the next year gets the same 0.4%-of-salary annual pension, if not less (because of discounting).

Much of the plaintiffs' argument rests on the idea that the account of a 25-year-old worker does not get 5% plus periodic interest, but instead is immediately credited with 5% of salary plus 40 years' interest. That makes the contributions look discriminatory: the 25-year-old worker's account receives 40 times as much interest credit in the year the contributions accrue as a 65-year-old worker's account. Once again, however, this perspective misunderstands both the statute and the time value of money.

Nothing in either ERISA or the IBM plan requires 40 years of interest to be credited to the account as soon as the young worker earns wages. What plaintiffs have in mind is the rule that, when any beneficiary (young or old) elects to take a cash distribution or roll the account into an annuity before reaching age 65, the plan must distribute a lump sum calculated to be the "actuarial equivalent" of the annuity that would be available at normal retirement age. ERISA § 204(c)(3), 29 U.S.C. § 1054(c)(3). To derive the "actuarial equivalent" of a pension at age 65, a plan must (a) add all interest that would accrue through age 65, then (b) discount the resulting sum to its present value. *Berger v. Xerox Corp. Retirement Income Guarantee Plan*, 338 F.3d 755, 762-63 (7th Cir.2003). Plaintiffs characterize step (a) as extra interest credits for the young, but they ignore step (b). The discount rate may be close to (if it does not exceed) the rate at which interest is imputed, so the amount paid out in cash may be close to if not below the nominal balance in the account. *Berger* did not consider

§ 204(b)(1)(H)(i) and does not hold that the process of grossing up the balance and then discounting is a form of age discrimination. To the contrary: *Berger* described this process as the means to *avoid* age discrimination.

As far as we can see, ours is the first appellate decision to address the status of cash-balance plans under § 204(b)(1)(H)(i). The class directs our attention to two decisions from other circuits that it says supply helpful analysis. *Miller v. Xerox Corp. Retirement Income Guarantee Plan*, 447 F.3d 728 (9th Cir.2006); *Esden v. Bank of Boston*, 229 F.3d 154 (2d Cir.2000). As the class reads them, these opinions stand for two important propositions. First, that an "accrued benefit" in a cash-balance plan is an annuity at normal retirement age. Second, that there is a "fundamental" distinction between defined-contribution and defined-benefit plans. Both of these propositions are correct, and both of them are irrelevant.

Start with the first proposition. What the true meaning of "accrued benefit" may be is not controlling; § 204(b)(1)(H)(i) does not use that phrase, and we have explained why "benefit accrual" means something other than "accrued benefit." Once we start to calculate accrued benefits for people who quit or retire early, it is necessary to impute extra interest and discount. *Berger* describes how this is done. But "benefit accrual" refers to the annual addition to the pot, not to the final payout. The holding of *Esden*, see 229 F.3d at 168, mirrors that of *Berger* and requires no further comment. *Miller* extends the framework of *Esden* and *Berger* to evaluate reductions in notional account balances caused by previous lump-sum distributions. 447 F.3d at 733-34. See 26 C.F.R. § 1.411(a)-7(d)(6) (offset may equal the "accrued benefit attributable to the distribution").

As for the second proposition, plaintiffs cite language describing the regulatory framework as "rigidly binary" (*Esden*, 229 F.3d 154, 159 n. 6). True enough. A defined-contribution plan entails fully funded individual accounts; everything else is a defined-benefit plan. 29 U.S.C. § 1002(25). *Miller* adds that "interest credits are defined benefit entitlements ... and are not analogous to the investment growth of a defined contribution plan." 447 F.3d at 735. Maybe so; that depends on what the court meant by "analogous." Interest in a defined-contribution plan is real, while interest credits in a defined-benefit plan are bookkeeping entries (effectively debt obligations of the employer to the extent that the pension trust fund does not cover them). But so what? IBM does not contend that its plan is governed *by* § 204(b)(2)(A), just that § 204(b)(1)(H)(i) does not whimsically require a court to find age discrimination for a defined-benefit plan when materially identical statutory language allows functionally identical defined-contribution plans to operate without any taint of discrimination. To say that defined-benefit and defined-contribution plans are governed by different subsections of ERISA is not to say that what is lawful for one must be forbidden to the other. We conclude that § 204(b)(1)(H)(i) and § 204(b)(2)(A) indeed provide similar treatment with respect to claims of age discrimination.

Only a brief mention of *Arizona v. Norris*, 463 U.S. 1073, 103 S.Ct. 3492, 77 L.Ed.2d 1236 (1983), another mainstay of the class's briefs, is called for. In *Norris* women making the same pension contributions as men, all else held equal, had lower annual pension benefits. *Id.* at 1082, 103 S.Ct. 3492. Under IBM's plan any differences in pension benefits are a function of differing years of service,

salary history, or the years the balance has been allowed to compound; age is not a factor.

Here, as so often, it is essential to separate age *discrimination* from other characteristics that may be correlated with age. That was the Supreme Court's point in *Hazen Paper*: wages rise with seniority (and thus with age) at many employers, but distinctions based on wage levels (in order to reduce a payroll) do not "discriminate" by age. See also, e.g., *Achor v. Riverside Golf Club*, 117 F.3d 339, 341 (7th Cir.1997) (need to show "the effect of age, isolated from other influences"); *Sheehan v. Daily Racing Form, Inc.*, 104 F.3d 940, 942 (7th Cir.1997) (expert should correct for "potentially explanatory variables other than age" when determining whether discrimination was because of age). While those decisions involved different statutory regimes, the objective is general: a plaintiff alleging age discrimination must demonstrate that the complained-of effect is *actually* on account of age. One need only look at IBM's formula to rule out a violation. It is age-neutral.

Now this may give a clue about why plaintiffs (a class of older workers) have sued. The cash-balance plan replaced a more traditional arrangement under which the annual pension on retirement was a function of closing salary (say, an average of the last five years before retirement) multiplied by the number of years of service. Because wages rise with seniority, such a formula favors older workers. Workers who quit or retire early not only miss out on the rising wages that accompany seniority but also don't receive credit for the time value of money: years of service at age 30 and at age 70 count equally in the traditional formula. Many employers design such back-loaded systems to give the most-experienced members of

the labor force a reason (even beyond rising salary) to stay on the job. Like a defined-contribution plan, a cash-balance plan removes the back-loading of the pension formula; older workers (accurately) perceive that they are worse off under a cash-balance approach than under a traditional years-of-service-times-final-salary plan. But removing a feature that gave extra benefits to the old differs from discriminating against them. Replacing a plan that discriminates against the young with one that is age-neutral does not discriminate against the old.

There is a transition issue. When IBM moved employees from a more traditional plan to a cash-balance system, it gave them the greater of the present value of their pension entitlements as of the transition date or the account balance that they would have had if IBM had a cash-balance plan in effect since the employee came to work. Plaintiffs complain that this gives the younger workers too much credit for interest (because more time passes between their work and retirement dates), but that rehashes arguments that we've already rejected. Every employee with the same salary and service record receives the same opening account balance under the new plan. That the change disappointed expectations is not material. An employer is free to move from one legal plan to another legal plan, provided that it does not diminish vested interests – and this transition did not. Cf. *Lockheed Corp. v. Spink*, 517 U.S. 882, 116 S.Ct. 1783, 135 L.Ed.2d 153 (1996) (employers are not fiduciaries under ERISA when they create or amend pension plans).

Litigation cannot compel an employer to make plans more attractive (employers can achieve equality more cheaply by reducing the highest benefits than by increasing the lower ones). It is possible, though, for litigation

about pension plans to make everyone worse off. After the district court's decision IBM eliminated the cash-balance option for new workers and confined them to pure defined-contribution plans. See Ellen E. Schultz & Theo Francis, *How Safe Is Your Pension? – Freeze of IBM Plan Leaves Workers Worrying If Their Employer Is Next*, Wall St. J., Jan. 12, 2006, at D1; Ellen E. Schultz, *IBM to Exclude New Workers From Its Cash-Balance Pension – Move to Only 401(k) Plans Follows Legal Questions*, Wall St. J., Dec. 9, 2004, at A2. Whether that is good or bad (for employees or society as a whole) is not for us to say. What we can and do conclude, however, is that the decision may again be made freely, governed by private choice rather than legal constraint.

The judgment of the district court is reversed, and the case is remanded with directions to enter judgment in IBM's favor.

**Kathi COOPER, Beth Harrington, and Matthew Hillesheim, Individually and on Behalf of All Those Similarly Situated, Plaintiffs,**

**v.**

**The IBM PERSONAL PENSION PLAN and IBM Corporation, Defendants.**

**No. CIV. 99-829-GPM.**

United States District Court,
S.D. Illinois.

July 31, 2003.

Steven A. Katz, Douglas R. Sprong, Korein Tillery, Swansea, IL, Robert F. Hill, John H. Evans, Hill & Robbins, William K. Carr, Law Offices of William K. Carr, Denver, CO, for Plaintiffs.

Jeffrey G. Huvelle, Robert D. Wick, Covington & Burling, Washington, DC, Frederick J. Hess, Lewis, Rice et al., Belleville, IL, for Defendants.

***MEMORANDUM AND ORDER***

**MURPHY, Chief Judge:**

The Cooper class challenges IBM's pension plan ("Plan") as violative of the age discrimination prohibitions of the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. §§ 1001-1461. All pending motions are listed in the appendix to this Memorandum and Order. (*See* Appendix A.)

## I. *Factual Background*

Plaintiff Cooper has been a Plan participant since May 21, 1979, the day she began her employment with IBM. Plaintiff Harrington was a Plan participant from 1990 to August 2000, when she terminated her employment with IBM. Towards the end of Harrington's employment, her pension benefits accrued pursuant to a Plan amendment made effective July 1, 1999. Plaintiff Hillesheim began employment with IBM in 1996 and terminated his employment in March 2000. He is a Plan participant, but because he was employed for fewer than five years, the benefits he accrued under the Plan did not vest.

### IBM Plan Amendments

The IBM Plan is a defined benefit pension plan[1] that provides benefits for IBM employees. Since 1995, the Plan has been amended twice. The changes created by these amendments are the basis of Plaintiffs' lawsuit.

### A. *The January 1, 1995 Amendment*

Before 1995, the IBM Plan provided benefits in the form of a lifetime annuity and a cash balance accumulation. On January 1, 1995, IBM's Board of Directors enacted an amendment to the Plan which adopted a plan

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[1] Under a conventional defined benefit plan, an employee is credited with a specific percentage of his or her salary for each year of employment. *See Esden v. Bank of Boston*, 229 F.3d 154, 158 n. 4 (2nd Cir.2000). This differs from a defined contribution plan in which funds are actually deposited into an employee's account.

design known as a pension equity plan. IBM coined its new design the Pension Credit Formula ("PCF").

PCF participants accrue a normal retirement benefit payable in the form of a life annuity commencing at age 65. Each year, a participant earns a specific number of "base points," which is determined by the employee's age in the year worked. Additionally, a participant can earn "excess points" if his or her five year average earnings are above social security compensation. Under this framework, however, a participant is permitted to accumulate no more than 425 base points and 75 excess points.

A participant's base points and excess points are applied to a five step formula to determine the monthly retirement benefit at age 65. Under this formula, a participant's base points are added, divided by 100, and multiplied by the average of his or her highest consecutive five year earnings. Then, after accounting for the participant's excess points, that number is divided by a "benefit conversion factor."

The class claims that the PCF violates ERISA because it is age discriminatory. This claim is based on the PCF's benefit conversion factor which increases in direct correlation to an employee's age. According to the class, this increase causes an older employee to receive a lower rate of benefit accrual and to have a smaller accrued benefit at age 65 than a younger employee, despite having worked the same number of years at the same salary as the younger employee.

### B. *The July 1, 1999 Amendment*

Effective July 1, 1999, IBM again amended its Plan to create its Cash Balance Formula ("CBF"). Under the CBF, a participant's benefit is determined by reference to a hypothetical account known as a Personal Pension Account ("PPA"). Every month, a participant's PPA accumulates "pay credits" at a rate of 5% of the employee's salary and "interest credits" at a rate one percentage point higher than the rate of return on one year treasury securities. When a participant's employment with IBM ends, he may withdraw his account balance as a lump sum, convert the account balance into an immediate life annuity, or defer the receipt of a lump sum payment or a life annuity until a later date. While a former employee is unable to earn additional pay credits, he continues to accumulate interest credits until his PPA balance is withdrawn or converted into a life annuity.

The class alleges that the CBF also violates ERISA's laws against age discrimination. This claim is based on how interest credits accrue on a participant's PPA balance until he reaches normal retirement age.

## II. *Standard of Review*

All but one of the motions before the Court are motions for summary judgment. The standard applied to summary judgment motions filed under Federal Rule of Civil Procedure 56 is well-settled and has been succinctly stated as follows:

> Summary judgment is proper when the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to

> any material fact and that the moving party is entitled to a judgment as a matter of law. In determining whether a genuine issue of material fact exists, [the court] must view the record in a light most favorable to the nonmoving party. Because the primary purpose of summary judgment is to isolate and dispose of factually unsupported claims, the nonmovant may not rest on the pleadings but must respond, with affidavits or otherwise, setting forth specific facts showing that there is a genuine issue for trial. The evidence must create more than some metaphysical doubt as to the material facts. A mere scintilla of evidence in support of the nonmovant's position is insufficient; a party will be successful in opposing summary judgment only when it presents definite, competent evidence to rebut the motion.

*Albiero v. City of Kankakee,* 246 F.3d 927, 931-32 (7th Cir.2001) (internal citations and quotations omitted).

## III. *Analysis*

The Court's analysis will be divided into two sections: (1) all motions related to IBM's 1995 Pension Credit Formula; and (2) all motions related to IBM's 1999 Cash Balance Formula.

### 1995 Pension Credit Formula

The class alleges that the terms of the IBM Plan, as amended January 1, 1995, violate ERISA § 204(b)(1)(G) & (H). Specifically, the class claims that under the PCF, benefits are reduced on account of *increases in age or service* in violation of § 204(b)(1)(G) and that the benefits accrue at a *rate which is reduced because of age or the*

*attainment of any age* in violation of § 204(b)(1)(H). The class seeks to have Plan benefits determined in a manner consistent with these ERISA provisions and to enjoin IBM from continuing these violations.

Defendants move to dismiss the § 204(b)(1)(H) claim on the grounds that the ERISA age discrimination provisions apply only to employees who have reached normal retirement age (age 65), arguing that the younger Plaintiffs lack standing to sue. Defendants are wrong.

ERISA § 502(a) provides that "[a] civil action may be brought . . . (3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this subchapter or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provision of this subchapter or the terms of the plan." 29 U.S.C. § 1132(a). The plain language of this provision confers statutory standing to plan participants, such as the named Plaintiffs, who seek to protect their employee benefit rights. Because Congress is entitled to enact statutes which create standing where it would otherwise not exist, *see Village of Bellwood v. Dwivedi,* 895 F.2d 1521, 1526 (7th Cir.1990), Defendants' motion to dismiss (Doc. 103) is denied.

### A. *§ 204(b)(1)(G) Claim*

Cooper filed a motion for partial summary judgment (Doc. 87) on July 18, 2002, seeking, in part, a determination that the PCF violates the age discrimination provision of ERISA § 204(b)(1)(G) because the amount of an employee's accrued benefit under the Plan decreases on account of the employee's age. Defendants have likewise filed a motion for summary judgment on the § 204(b)(1)(G)

claim, arguing that no participant in the IBM Plan has ever experienced a reduction in his or her accrued benefit on account of an increase in age or service and, therefore, the named Plaintiffs lack standing to assert this claim.

Section 204(b)(1)(G) has been part of ERISA since its inception in 1974 and provides that "a defined benefit plan shall be treated as not satisfying the requirements of this paragraph if the participant's accrued benefit is reduced on account of any increase in his age or service." 29 U.S.C. § 1054(b)(1)(G). In the context of a defined benefit plan, such as the IBM Plan, the term "accrued benefit" means "'the individual's accrued benefit determined under the plan and . . . *expressed in the form of an annual benefit commencing at normal retirement age.*'" 29 U.S.C. § 1002(23)(A). "Normal retirement age" is 65. *See* 29 U.S.C. § 1002(24); *see also Esden v. Bank of Boston*, 229 F.3d 154, 162 (2nd Cir.2000).

The PCF adopted by IBM in the January 1, 1995, amendment to its Plan violates ERISA. The following examples illustrate the violation.

A participant's retirement benefit is computed under the PCF by a five step formula: (1) the total number of base points earned at that time, up to a maximum of 425, are added and then divided by 100; (2) the number from the first step is multiplied by the average of the employee's highest consecutive five year earnings to determine what the Plan denominates as the "Base Point Benefit Value at Normal Retirement Age;" (3) if the employee's five year average earnings exceed social security compensation, the excess points earned are similarly added, up to a maximum of 75, divided by 100, and then multiplied by the dollar amount by which the employee's five year average

exceeds social security compensation, to determine the employee's "Excess Point Benefit Value at Normal Retirement Age;" (4) the employee's Base Point Benefit Value at Normal Retirement Age and any Excess Point Benefit Value at Normal Retirement Age are added together to yield the employee's "Pension Credit Value at Normal Retirement Age;" and (5) this Pension Credit Value is then divided by a "Benefit Conversion Factor" specified in the Plan. The result is the dollar amount of the employee's annual annuity commencing at age 65, which can be divided by twelve to determine the monthly annuity.

Suppose an employee begins working for IBM at age 35 and earns an annual salary of $60,000.00 until his employment ends at age 50. During this fifteen year period, he will accumulate 215 base points. *See* App. B. After dividing by 100, and multiplying by $60,000.00, the employee is assigned a "Base Point Benefit Value at Normal Retirement Age" of $129,000.00. Because termination occurs when this employee is 50 years old, his benefit conversion factor (which is divided into his $129,000.00 base point value) is 8.537. *See* App. C. Therefore, his age 65 accrued benefit is equal to **$15,110.69 per year or $1,259.22 per month**.

Now, change only the age – our hypothetical employee starts his employment with IBM at age 50 instead of age 35. This employee will accumulate more base points than his younger counterpart; a total of 240. *See* App. B. After dividing by 100, and multiplying by $60,000.00, he is assigned a higher "Base Point Benefit Value at Normal Retirement Age" of $144,000.00. However, this 65 year old employee is also assigned a higher benefit conversion factor equal to 10.918. *See* App. C. After his $144,000.00 base point value is reduced by this conversion factor, he is

left with an age 65 accrued benefit equal to only **$13,189.23 per year or $1,099.10 per month.**

Finally, consider an employee who begins working at age 25 and earns $60,000.00 each year until he retires at age 65. By age 58, this employee has 423 base points and a benefit conversion factor of 10.543. *See* Apps. B & C. Applying the PCF's five step analysis, he has an age 65 accrued benefit of **$24,072.84 per year or $2,006.07 per month**. For an additional year of service, this same employee will receive only two (as opposed to sixteen) base points because he will have reached the 425 point cap. Notwithstanding, the employee's benefit conversion factor continues to rise to 10.596. *See* App. C. After applying the IBM formula, his age 65 accrued benefit has *decreased* to **$24,065.69 or $2,005.47 per month**. Each additional year he works, this employee will accumulate zero base points because of the cap. Still, as his years of service continue to increase, so does the benefit conversion factor. By age 65, this employee's benefit conversion factor will be 10.918. *See* App. C. Under the PCF, this will yield an accrued benefit of only **$23,355.93 or $1,946.00 per month**.

The benefit conversion factor contained in the PCF reduces a participant's accrued benefit solely on increases in age or service. Accordingly, the 1995 PCF violates ERISA § 204(b)(1)(G). *See* 29 U.S.C. § 1054(b)(1)(G). Defendants' argument that no specific employee has actually suffered a reduction in his or her accrued benefit is rejected because it relates to damages as opposed to liability and because Congress has conferred statutory standing to all "participants" in an ERISA plan. *See* 29 U.S.C. § 1132(a)(3). Plaintiffs' motion for partial summary judgment on Count

I (Doc. 87) is granted, and Defendants' motion for partial summary judgment on Count I (Doc. 105) is denied.

### B. *§ 204(b)(1)(H)*

Cooper's motion for partial summary judgment on Count I also seeks a determination that the PCF in the 1995 IBM Plan violates ERISA § 204(b)(1)(H) because the rate of an employee's benefit accrual under the Plan decreases on account of the employee's age. Defendants have also filed a motion for summary judgment on the § 204(b)(1)(H) claim.

Section 204(b)(1)(H) was enacted as part of the Omnibus Budget Reduction Act of 1986 and provides that "a defined benefit plan shall be treated as not satisfying the requirements of this paragraph if, under the plan, an employee's benefit accrual is ceased, or the rate of an employee's benefit accrual is reduced, because of the attainment of any age." 29 U.S.C. § 1054(b)(1)(H).

Under the PCF, the rate of accrual of an employee's *immediately-payable* benefit steadily increases with age. However, the PCF can result in a decrease in the rate at which an employee's *age 65 annuity* accrues. Therefore, it is important whether § 204(b)(1)(H)'s term "rate of benefit accrual" refers to the rate at which an employee accrues a benefit payable in the form of an annuity that commences at age 65, or if an employee's "rate of benefit accrual" may be measured by reference to an immediate annuity.

ERISA does not explicitly answer this question. However, the term "accrued benefit" which appears in § 204(b)(1)(G) refers to an employee's accrued benefit "expressed in the form of an annual benefit commencing at

normal retirement age." *See* 29 U.S.C. § 1002(23)(A); *see also Esden,* 229 F.3d at 163. Defendants argue that § 204(b)(1)(H)'s phrase "rate of benefit accrual" should not be expressed in the form of an age 65 benefit and that the term *benefit accrual* means something different than the term *accrued benefit.*

This argument is based on the actuarial premise "time value of money." According to Defendants, it is economically nonsensical to compare a 25 year old employee's rate of benefit accrual with a 64 year old employee's rate of benefit accrual by reference to the age 65 benefit that each has accumulated, because the 64 year old employee is set to receive his benefit much sooner. Accordingly, § 204(b)(1)(H)'s phrase "rate of benefit accrual" should be interpreted to refer to benefits payable immediately upon termination of employment.

From an economist's perspective, Defendants have a good argument. A dollar today is worth more than the promise of a dollar a year from now. This does not mean, however, that the PCF is legal.

ERISA creates specific rules relating to defined benefit plans. It is clear that a participant's accrued benefit, as it appears in § 204(b)(1)(G), must be measured by reference to the amount of an employee's annual benefit at age 65. *See* 29 U.S.C. § 1002(23)(A); *see also Esden,* 229 F.3d at 163. The language at issue – "rate of benefit accrual" – is found in the very next subchapter, § 204(b)(1)(H). The best interpretation of this phrase is that it also refers to an employee's age 65 annual benefit and the rate at which that age 65 annual benefit accrues.

Defendants question why Congress would use different language in succeeding subparagraphs (accrued

benefit and benefit accrual) unless it intended the subparagraphs to cover different types of benefits. The answer is simple. Congress chose to be grammatically correct. The term accrued benefit in § 204(b)(1)(G) means an employee's age 65 *accumulated benefit.* If Congress had used the term accumulated benefit in § 204(b)(1)(G), instead of the term accrued benefit, it would not have used the clumsy phrase "rate of accumulated benefit" in § 204(b)(1)(H). Presumably, Congress would have opted for standard English and used the phrase "rate of benefit accumulation," even though it intended to cover the same type of benefit in both subparagraphs.[2]

Congress intended § 204(b)(1)(H) to cover the rate at which a participant's age 65 benefit accrues under a defined benefit plan. So, is the rate of a participant's benefit accrual under the PCF reduced because of the participant's age? The answer is yes, as illustrated by the previous hypotheticals.

A participant who works at IBM from age 35 to age 50 earning a salary of $60,000.00 will accrue an age 65 annual benefit under the PCF of **$15,110.69**. On the other hand, an employee who works for IBM from age 50 to age 65, also earning an annual salary of $60,000.00, will accrue an age 65 annual benefit under the PCF of only **$13,189.23**. To determine the "rate of benefit accrual" for these hypothetical employees, their age 65 annuity is divided by the product of their average compensation

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[2] For a simpler example, consider the word popcorn. Popcorn is the word used to describe the product created by exposing corn kernels to extreme heat. If asked to draft a phrase related to the speed of this process, one would not say "rate of popcorn." Rather, to be grammatically correct, one would say "the rate corn pops."

($60,000.00) and years of service (15). *See* Doc. 88, App. C, p. 11. Thus, the 50 year old employee accrues an age 65 annual benefit at a rate of **1.68%**.[3] In contrast, the 65 year old employee accrues an age 65 annual benefit at a rate of only **1.47%**.[4]

The decrease in rate of age 65 annual benefit accrual is also demonstrated by reference to the sharp yearly reduction in percentage that occurs to employees who have reached the 425 base point cap under the PCF. As previously noted, an employee who begins working for IBM at age 25 will reach the 425 base point maximum between ages 58 and 59. At age 59, after 35 years of service, he has accrued an age 65 annual benefit of $24,065.69 [5] under the PCF. Therefore, his rate of benefit accrual is **1.15%**.[6] At age 60, with an annual benefit of $23,945.91, his rate of benefit accrual drops to **1.11%**.[7] This employee's rate of benefit accrual continues to decrease each year, leaving him with a rate of **0.95%**[8] by age 65.

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[3] $15,110.68/($60,000.00 x 15).

[4] $13,189.23/($60,000.00 x 15).

[5] This employee has accumulated 425 base points and has a benefit conversion factor of 10.596. See Apps. B and C. Because his highest five year average salary is $60,000.00, the PCF would be applied as follows:

(425/100) = 4.25 x $60,000.00 = $255,000.00/10.596 = $24,065.69
4.25 $255,000.00

[6] Again, rate of benefit accrual is calculated by dividing an employee's age 65 annual benefit by (years of service x average compensation):

$24,065.69/(35 x $60,000.00) or
$24,065.69/($2,100,000.00) = 1.15%

[7] $23,945.91/(36 x $60,000.00) or
$23,945.91/($2,160,000.00) = 1.11%

[8] $23,355.93/(41 x $60,000.00) or
$23,355.93/(2,460,000.00) = 0.95%

These examples illustrate that under the PCF, a participant's rate of benefit accrual decreases because of the attainment of a certain age. For this reason, the PCF violates ERISA § 204(b)(1)(H). Plaintiffs' motion for partial summary judgment on Count I (Doc. 87) is granted, and Defendants' motion for partial summary judgment on Count I (Doc. 130) is denied.

### C. *§ 204(b)(1)(A)(B) & (C) (Anti-backloading)*

The class also claims that, effective January 1, 1995, benefits accruing under the terms of the IBM Plan do not satisfy any of the three "anti-backloading" rules found in subparagraphs (A), (B), or (C) of ERISA § 204(b)(1). *See* 29 U.S.C. § 1054(b)(1). Defendants seek summary judgment on this claim. Defendants cannot comply with either the 3% rule or the 133 1/3% rule and must comply with the anti-backloading rules, if at all, by satisfying the fractional rule of § 204(b)(a)(C).

The issue is whether the Plan's PCF satisfies subparagraph (C) during its "phase-in" period from January 1, 1995 (the date of the PCF's enactment) to December 31, 1999.

ERISA § 204(b)(1)(C) states:

> [a] defined benefit plan satisfies the requirements of this paragraph if the accrued benefit to which any participant is entitled upon his separation from the service is not less than a fraction of the annual benefit commencing at normal retirement age to which he would be entitled under the plan as in effect on the date of his separation if he continued to earn annually until normal retirement age the same rate of compensation upon

> which his normal retirement benefit would be computed under the plan, determined as if he had attained normal retirement age on the date any such determination is made (but taking into account no more than the 10 years of service immediately preceding his separation from service). Such fraction shall be a fraction, not exceeding 1, the numerator of which is the total number of his years of participation in the plan (as of the date of his separation from the service) and the denominator of which is the total number of years he would have participated in the plan if he separated from the service at the normal retirement age. For purposes of this subparagraph, social security benefits and all other relevant factors used to compute benefits shall be treated as remaining constant as of the current year for all years after such current year.

29 U.S.C. § 1054(b)(1)(C).

A 40 year old employee starts working for IBM on January 1, 1995, with an annual salary of $60,000.00 and quits one year later. His accrued annual benefit is **$311.80.**[9] To satisfy § 204(b)(1)(C), his "fractional rule

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[9] Under the terms of the IBM Plan, the PCF uses compensation averaged over a five year period. However, compensation earned before 1995 cannot be used in this average. Therefore, from January 1, 1995, to December 31, 1999, a participant's average compensation is determined by adding together his total compensation and dividing by five. In the hypothetical above, the employee earning $60,000.00 per year has an average compensation of only $12,000.00 after his first year of service. The employee accumulated 15 base points and has a conversion factor of 5.773. *See* Apps. B & C. Using these figures, the analysis under the PCF is as follows:

| | | | |
|---|---|---|---|
| (15/100) = .15 | .15 x $12,000.00 = $1,800.00 | $1,800.00/5.773 = | $311.80 |

benefit" (the age 65 annual accrued benefit to which he would be entitled under the PCF if he continued to earn $60,000.00 annually until he attained age 65, multiplied by the applicable fraction) must be less than or equal to $311.80. His annual accrued benefit is **$21,707.27**[10] if he continues working until age 65. The fraction used to reduce this amount is **1/25.**[11] Thus, his fractional rule benefit is **$868.29,**[12] an amount greater than the benefit accrued on the date he stopped working for IBM. This violation continues until the fourth year (1998) of the PCF's "phase-in" period.[13]

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[10] This employee would accumulate 395 base points and would have a conversion factor of 10.918 if he continues working until age 65. *See* Apps B and C. Because under § 204(b)(1)(C) it is presumed that he continues earning $60,000.00 until age 65, the PCF would be applied as follows:

$$(395/100) = \frac{3.95}{3.95} \times \$60{,}000.00 = \$237{,}000.00 \qquad \$237{,}000.00/10.918 = \underline{\$21{,}707.27}$$

[11] $$\frac{\text{Total \# of years of participation in the plan (as of date of separation from service)}}{\text{Total \# of years he would have participated in the plan if he separated from the service at the normal retirement age.}}$$

[12] $21,707.27 x (1/25) = $868.29.

[13]

| | | | |
|---|---|---|---|
| *1996*: | Benefit on date of separation | = $1,187.73 | [(30/100 x $24,000.00)/6.062] |
| | Fractional rule benefit | = $1,736.58 | ($21,707.27 x 2/25) |
| *1997*: | Benefit on date of separation | = $2,545.17 | [(45/100 x $36,000.00)/6.365] |
| | Fractional rule benefit | = $2,604.87 | (21,707.27 x 3/25) |
| *1998*: | Benefit on date of separation | = $4,309.44 | [(60/100 x $48,000.00)/6.683] |
| | Fractional rule benefit | = $3,473.12 | (21,707.27 x 4/25) |

But Defendants argue that § 204(b)(1)(C)'s language "as if he had attained normal retirement age on the date any such determination is made" should be interpreted to mean that the fractional rule benefit should be calculated as though the employee turned age 65 on the date his service ended. This is wrong.[14] Section 204(b)(1)(C) provides that the fractional rule benefit is the "annual benefit commencing at normal retirement age to which [an employee] would be entitled ... if he *continued to earn annually until normal retirement age* the same rate of compensation upon which his normal retirement benefit would be computed under the plan." (emphasis added). The words *continued to earn annually until normal retirement age* means that the employee's benefit must be calculated as though he remained employed until age 65.

Moreover, if Defendants' interpretation is correct, § 204(b)(1)(C) is rendered meaningless. The 40 year old hypothetical employee used in the last example would have a fractional rule benefit of **$7.03**[15] at the end of his

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[14] For the reasons that follow in the text of this Order, § 204(b)(1)(C), when read as a whole, does not call for a fractional rule benefit calculated as though an employee turned age 65 on the date his service ended. The Court reads the phrase "as if he had attained normal retirement age on the date any such determination is made" as referring solely to an employee's rate of compensation, and is included to ensure that the salary that an employee is earning when his service ends is used as the employee's salary at age 65 when his fractional rule benefit is determined.

[15] If the employee retired in 1996, after working only one year, he would be treated as having turned age 65 in 1996 for fractional rule purposes if Defendants have correctly interpreted § 204(b)(1)(G). Therefore, he would have accumulated 16 base points during this year of employment and would have a conversion factor of 10.918 under the PCF. *See* Apps. B and C. Thus, his fractional rule benefit would be calculated as follows:

(Continued on following page)

first year of employment as Defendants apply the statute. Congress did not intend § 204(b)(1)(C) to invalidate only those plans that produce less than $7.03 in pension benefits for a 40 year old employee earning $60,000.00.

Defendants argue that it is unfair to compare a partially phased in benefit with a fully phased in fractional rule benefit. But this is exactly the situation that § 204 is intended to cover. *See Jones v. UOP,* 16 F.3d 141, 144-45 (7th Cir.1999). The PCF directs that a first year participant's salary be divided by five and accordingly that participant's benefits are "backloaded," *i.e.,* five years of employment are required before the participant can ratably accrue pension benefits. Defendants' motion for summary judgment on the § 204(b)(1)(C) claim (Doc. 128) is denied.

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(16/100) = .16 .16 x $12,000.00 = $1,920.00 $1,920.00/10.918 = $175.86

$175.86 x 1/25 = $7.03

In determining the applicable fraction, the Court uses a denominator that is determined by subtracting the employee's age when participation in the Plan began from age 65. Defendants may assume that based on their theory – a fractional rule benefit is calculated as though an employee turned age 65 on the date his service ended – the denominator in the applicable fractions should be determined by counting to age 65 as though the employee reached such age on the date employment was terminated. This assumption is unsupportable. If the applicable fraction used a denominator that counted forward only to the date that an employee's service ended, the fraction would always be one, a result that cannot be supported by § 204(b)(1)(C)'s language. To illustrate that the fraction would always be one (and thus there would be no reason for § 204(b)(1)(C) to instruct the usage of a fraction), again consider the hypothetical forty year old. If his service ends in 1998, the numerator will be three (number of years of participation in the Plan). The denominator would also be three because, by treating the employee as if he turned 65 at termination, there are no more years to add by assuming the employee continued working to normal retirement age.

***THE CASH BALANCE PLAN***

The 1995 PCF was intended to provide a rapid build up of plan value for young and mid-career hires while reducing generous early retirement subsidies. The PCF worked well, and by 1998 IBM had over 20,000 employees between 35 and 55 years of age who had fewer than five years of service. So, in 1998 IBM faced rising pension costs and diminishing pension income as a result of the benefits the company would be paying to their middle aged employees. But, the Plan was not strapped for cash, as there was a surplus of $8 billion at the close of 1997, and the Plan's assets were generating a return greater than what was required to cover the annual costs of providing benefits. Although IBM had not contributed to the Plan for several years, in 1997, 7% of IBM's total reported net earnings was pension income in the amount of $420 million.

In 1999 IBM again amended the Plan and opted for a "cash balance formula" whereby a participant's benefit is determined by reference to a hypothetical account. The Plan's actuaries projected that this CBF would produce annual savings of almost $500 million by 2009. These savings would result from reductions of up to 47% in future benefits that would be earned by older IBM employees.

IBM was aware of the age discrimination issues that would come with the new CBF. Indeed, the Plan's actuaries projected the age 65 annuity benefit earned by a younger employee for a year of service exceeded the benefit earned by an older employee for the same service. And, the actuaries calculated that the amount of an age 65 annuity earned each year by an employee under the CBF

decreased as the employee aged. Nevertheless, the new CBF went into effect July 1, 1999. Due to negative reaction from employees, the Plan was amended a second time in September 1999 to permit more employees to choose between being covered by the new formula or the previous formula.

The CBF had its intended effect. Plan income increased from $395 million in 1998 to $638 million in 1999. Astonishingly, Plan income was over $1 billion in 2001, and this accounted for 13% of IBM's overall net income.

The parties agree that the 1999 Plan as amended is a defined benefit plan. Therefore, the Plan must comply with the many and complex statutory strictures that apply to all defined benefit plans. IBM presents startling anomalies and absurdities that result from pushing the logic that Plaintiffs develop in their argument. But these anomalies and absurdities occur only because the CBF doesn't work within the longstanding statutory framework regarding defined benefit plans. The 1999 Plan looks like a defined contribution plan trying to pass for a defined benefit plan. It doesn't make the cut.

Before testing the CBF under ERISA § 204(b)(1)(H), it is helpful to compare the two types of pension plans authorized by ERISA. A defined contribution plan is easy to describe and understand. The sponsoring employer contributes a specified amount into a separate account for each employee. The risks and rewards of the investment are borne by the employee. The employer does not guarantee a particular result and is off the hook. However, there is no opportunity for the employer to earn pension income or reduce the real costs of the contributions specified in the plan. In this type of plan, the sponsoring employer's

performance is measured by what it puts into the plan. A defined benefit plan is a different creature. The sponsoring employer promises a certain result based upon a formula specified in the plan. The employer must deliver on the promise irrespective of how the funds set aside for this purpose fare in the financial markets. Here, the employer is literally on the hook but has the opportunity to earn pension income and reduce the real costs of funding a pension for employees. In this type of plan, the sponsoring employer's performance is measured by what comes out of the plan in terms of benefits.

### A. *Section 204(b)(1)(H)*

The CBF adopted by the 1999 amendment to the Plan creates a hypothetical account referred to as a personal pension account ("PPA") for each participant. Benefits accrue by the addition of "pay credits" and "interest credits" made to the participant's PPA. Future interest payments are guaranteed by the Plan irrespective of a participant's continued employment with IBM.

It is settled that a cash balance plan such as the IBM Plan is held to the same requirements regarding vesting and accrual of benefits as any defined benefit plan. *Esden,* 229 F.3d at 162-63. For each year of qualifying service, such a plan must provide for a definitely determinable, non-forfeitable, "accrued benefit." ERISA § 203(a). The accrued benefit must be expressed in the form of an annual benefit commencing at normal retirement age. 29 U.S.C. § 1002(23). Moreover, the interest credits that are projected and valued as an age 65 annuity must also be taken into account in determining whether a cash balance plan complies with the benefit accrual requirements under

ERISA § 204(b)(1). *Esden,* 229 F.3d at 166, n. 18. This is where the CBF runs afoul of ERISA's age discrimination proscriptions.

Interest credits are a part of the accrued benefit specified in IBM's 1999 Plan, and these count in determining whether the benefit accrual requirements of § 204(b)(1) are met. And, like in any defined plan, the interest credits must be valued as an age 65 annuity. At this point in the analysis, the result is inevitable. In terms of an age 65 annuity, the interest credits will always be more valuable for a younger employee as opposed to an older employee. A noted pension expert summarized matters:

> There is no dispute about the underlying arithmetic of cash balance arrangements: each year, as a cash balance participant ages, the same contribution made for her in the previous year declines in value in annuity terms. Moreover, cash balance arrangements are defined benefit plans and, therefore, measure accrued benefits in terms of annuities, not in terms of the contributions themselves.

Edward A. Zelinsky, *The Cash Balance Controversy,* 19 Virginia Tax Rev. 4, 733 (Spring 2000).

The 1999 CBF violates the literal terms of ERISA § 204(b)(1)(H). IBM's own age discrimination analysis illustrates the problem: a 49 year old employee with 20 years of service accrues an age 65 annuity of $8,093 in the year 2000. The following year, he accrues an additional $622, and by 2010, his additional annual accrual is only $282. This 49 year old employee's benefit accrual has been reduced for each year he has aged, and this reduction violates ERISA § 204(b)(1)(H).

IBM's argument that this example merely illustrates the time value of money at work collapses when the age 65 annuity is included in the analysis. The rate of a participant's benefit accrual diminishes as the participant closes on the age 65 target. And, age 65 is normal retirement age, and Congress did not intend the term "benefit accrual" to mean something different from "accrued benefit." The syntax differs ever so slightly so as to comport with the requirements of good English usage, but the concept is exactly the same.

ERISA does not require an employer to provide a pension plan at all, nor does it favor one type of plan over another. The question is not whether a CBF is a "good" thing. IBM could have accomplished what it has to date by terminating the defined benefit plan and moving to a defined contribution plan According to IBM, this was impractical as the Plan surplus could not have been "tax effectively" withdrawn; but, the point stands. There is nothing in ERISA to prevent IBM from moving to a defined contribution plan that functions like the CBF. There may be policy reasons why Congress should specifically authorize CBFs in the context of defined benefit plans. But the narrow question here is whether the 1999 Plan comports with the literal and unambiguous provisions of ERISA § 204(b)(1)(H), and it does not.

In short, IBM's argument goes to the wisdom of the statutory requirements that Congress adopted regarding defined benefit plans. These requirements were in effect before IBM considered adopting the CBF. IBM, like many other corporate plan sponsors, proceeded with open eyes and was fully informed of the consequences of the litigation that was sure to come. This Court will not perform legal legerdemain by dodging the detail requirements of

ERISA in order to save IBM's 1999 Plan. Plaintiffs' cross motion for summary judgment regarding the CBF adopted by the IBM Plan by an amendment effective July 1, 1999 (Doc. 124) is granted. IBM's cross motion for summary judgment on Plaintiffs' age discrimination claim (Doc. 105) is denied.

### B. *Partial Termination*

Defendants' motion for summary judgment on the issue of partial termination is denied because there is a genuine question of material fact (1) whether the July 1, 1999, amendment to the Plan resulted in a decrease in future benefit accruals, and (2) whether any such decrease increased the potential for a reversion. The effects of the subsequent amendment to the Plan which was adopted October 1, 1999, as IBM argues, may make the measurement of the effects of the change unreliable, but this itself constitutes a disputed material fact.

## IV. *Conclusion*

Accordingly, Plaintiffs' motion for partial summary judgment on Count I (Doc. 87) is **GRANTED**. Defendants' motion to dismiss for lack of standing (Doc. 103) is **DENIED**. Defendants' motion for summary judgment on the age discrimination claim (Doc. 105) is **DENIED**. Defendants' motion for summary judgment on the § 204(b)(1)(G) claim (Doc. 107) is **DENIED**. Plaintiffs' motion for summary judgment on the cash balance formula (Doc. 124) is **GRANTED**. Plaintiffs' motion for summary judgment on the opening account balance under the cash balance formula (Doc. 127) is **GRANTED**. Defendants' motion for summary judgment on the anti-backloading claim (Doc.

128) is **DENIED**. Defendants' motion for summary judgment regarding the pension credit formula (Doc. 130) is **DENIED**. Defendants' motion for summary judgment regarding partial termination is **DENIED**. Plaintiffs' appeal of the Magistrate's November 1, 2002, Order granting in part and denying in part the motion to compel discovery (Doc. 152) is **DENIED as moot** with leave to reinstate.

There is a triable issue of fact regarding Plaintiffs' anti-backloading claim as well as the partial termination claim. The parties will promptly proceed to develop the issue of what relief the Court should order.

**IT IS SO ORDERED.**

***APPENDIX A***

The following motions are before the Court:

(1) Plaintiffs' motion for partial summary judgment on Count I (Doc. 87);

(2) Defendants' motion to dismiss Plaintiffs' § 204(b)(1)(H) claim for lack of standing (Doc. 103);

(3) Defendants' motion for partial summary judgment on Plaintiffs' age discrimination claim (Doc. 105);

(4) Defendants' motion for summary judgment on Plaintiffs' § 204(b)(1)(G) claim (Doc. 107);

(5) Plaintiffs' cross motion for partial summary judgment on Plaintiffs' age discrimination claim with respect to Cash Balance Formula (Doc. 124);

(6) Plaintiffs' motion for partial summary judgment on Count I – comparison formula for opening balances under 1999 cash balance formula (Doc. 127);

(7) Defendants' motion for summary judgment on anti-backloading claim (Doc. 128);

(8) Defendants' motion for summary judgment on Plaintiffs' § 204(b)(1)(H) claim with respect to pension credit formula (Doc. 130);

(9) Defendants' motion for summary judgment on Plaintiffs' horizontal partial termination claim (Doc. 133), and

(10) Plaintiffs' appeal of the Magistrate's November 1, 2002, Order granting in part and denying in part the motion to compel discovery (Doc. 152).

***APPENDIX B***

| *Age in Each Year Worked* | *Base Points Earned Each Year* | *Excess Points Earned Each Year* |
|---|---|---|
| *Younger than 30* | *7* | *0* |
| *30-34* | *9* | *1* |
| *35-39* | *12* | *2* |
| *40-44* | *15* | *2* |
| *45 and Older* | *16* | *3* |

## *APPENDIX C*

| *Age at Termination* | *Benefit Conversion Factors* |
|---|---|
| *40* | *5.498* |
| *41* | *5.773* |
| *42* | *6.062* |
| *43* | *6.365* |
| *44* | *6.683* |
| *45* | *7.017* |
| *46* | *7.298* |
| *47* | *7.590* |
| *48* | *7.893* |
| *49* | *8.209* |
| *50* | *8.537* |
| *51* | *8.879* |
| *52* | *9.234* |
| *53* | *9.603* |
| *54* | *9.987* |
| *55* | *10.387* |
| *56* | *10.439* |
| *57* | *10.491* |
| *58* | *10.543* |
| *59* | *10.596* |
| *60* | *10.649* |
| *61* | *10.702* |

| | |
|---|---|
| *62* | *10.756* |
| *63* | *10.810* |
| *64* | *10.864* |
| *65* | *10.918* |

**IN THE UNITED STATES DISTRICT COURT**
**FOR THE SOUTHERN DISTRICT OF ILLINOIS**

| | | |
|---|---|---|
| **KATHI COOPER, BETH HARRINGTON, and MATTHEW HILLESHEIM, Individually and on Behalf of All Those Similarly Situated,** | ) | |
| **Plaintiffs,** | ) | **CIVIL NO. 99-829-GPM** |
| **vs.** | ) | |
| **THE IBM PERSONAL PENSION PLAN and IBM CORPORATION,** | ) | |
| **Defendants.** | ) | |

**JUDGMENT IN A CIVIL CASE**

(Filed Aug. 16, 2005)

**DECISION BY COURT.** This matter came before the Court on cross motions for summary judgment and a Class Action Settlement Agreement with Respect to Subclasses 1 and 2 ("Settlement Agreement"). The issues having been duly heard and a decision having been duly rendered,

**IT IS ORDERED AND ADJUDGED** that judgment is entered in favor of the members of Subclasses 1 and 2 on their claim that the Cash Balance Formula violates ERISA § 204(b)(1)(H). These Class Members are entitled to relief for the violation as provided in the Settlement Agreement.

**IT IS FURTHER ORDERED AND ADJUDGED** that judgment is entered in favor of the members of Subclasses 1 and 2 on their claim that the Always Cash Balance Formula violates ERISA § 204(b)(1)(H). These

Class Members are entitled to relief for the violation as provided in the Settlement Agreement.

**IT IS FURTHER ORDERED AND ADJUDGED** that the Plan shall pay Class Counsel fees as an administrative cost of the Plan in accordance with the Settlement Agreement and calculated on a decreasing percentage as follows: (1) an amount equal to 29% of the amount of any Settlement Benefits recovered up to $250 million; (2) an amount equal to 25% of the amount of any Settlement Benefits recovered in excess of $250 million up to the amount of $750 million; (3) an amount equal to 21% of the amount of any Settlement Benefits recovered in excess of $750 million up to the amount of $1,250 million; and (4) an amount equal to 17% requested of any Settlement Benefits recovered in excess of $1,250 million. Class Counsel shall pay incentive awards of $40,000 to Ms. Cooper and $20,000 to Ms. Harrington out of the attorneys' fees paid by the Plan and shall also reimburse themselves for any expenses they already have incurred or will incur in the future out of the attorneys' fees awarded by this Court.

**IT IS FURTHER ORDERED AND ADJUDGED** that the claims of Subclass 3 were dismissed pursuant to a Rule 54(b) judgment entered on January 10, 2005. All other claims asserted by Plaintiffs in this action are now **DISMISSED with prejudice** pursuant to the terms of the Settlement Agreement and in exchange for the consideration provided therein.

**DATED**: 08/16/2005

NORBERT G. JAWORSKI,
CLERK

By: s/ Linda M. Cook
Deputy Clerk

APPROVED: s/ G. Patrick Murphy
G. PATRICK MURPHY
CHIEF U.S. DISTRICT JUDGE

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

September 1, 2006

Before

**Hon.** WILLIAM J. BAUER, Circuit Judge

**Hon.** FRANK H. EASTERBROOK, Circuit Judge

**Hon.** DANIEL A. MANION, Circuit Judge

KATHI COOPER, *et al.*, on behalf of a class,

*Plaintiffs-Appellees*,

**No.** 05-3588 **v.**

IBM PERSONAL PENSION PLAN and IBM CORPORATION,

*Defendants-Appellants*.

Appeal from the United States District Court for the Southern District of Illinois.

No. 99-829-GPM
G. Patrick Murphy,
*Chief Judge*.

## Order

Plaintiffs-appellees filed a petition for rehearing and rehearing en banc on August 21, 2006. No judge in regular active service has requested a vote on the petition for rehearing en banc,* and all of the judges on the panel have voted to deny rehearing. The petition for rehearing is therefore DENIED.

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* Circuit Judges Kenneth F. Ripple, Ilana Diamond Rovner and Ann Claire Williams took no part in the consideration of this matter.